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Options for Sugar Trade in the Upcoming WTO Negotiations

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Ladies and Gentlemen, it is a pleasure to see all of you here at the Outlook Conference. With a lovely springtime coming here in the Washington area, the domestic and world sugar markets are in disarray with surplus supplies and depressed prices. And the world is about to embark on a new round of negotiations on agricultural reforms. It is a good thing the sun is shining and the air is fresh and warm. This morning, if I can resist going out to bask in the sun, I expect to offer my perspectives on whether the World Trade Organization (WTO) trade talks will yield real changes in sugar policies?

I believe there are two principal alternative scenarios for the outcomes of the new multilateral trade negotiations on agriculture that were recently authorized by the WTO General Council and will begin next month in Geneva in conjunction with the meetings of the Agriculture Committee. In the first scenario, the participants will agree to continue to use the Uruguay Round pattern of reductions and will agree to significant but modest further reductions. In the second scenario the participants will fail to agree on further reforms. Let's see how sugar would fare under these scenarios.

First, let's consider domestic support and the scenario of further cuts along the same lines as before. Domestic support was divided into three categories: amber, blue, and green, and reduction commitments were based on an Aggregate Measure of Support (AMS) for amber box policies.

The green box consists of non-trade distorting policies, like research and inspections and infrastructure, that are exempt from reduction. The United States claims that the Freedom to Farm production flexibility contract payments fall into the green box as decoupled income support. Of course, sugarcane and sugar beet growers don't receive such decoupled income support payments either in the United States or in Europe or anywhere else that I know.

The blue box consists of direct payments to farmers tied to production limits, such as the former U.S. deficiency payments for corn and wheat and other field crops which were subject to acreage reduction programs. The blue box payments were included in the base AMS from which reduction commitments are calculated, but such payments are exempt from reduction. This was a smoke and mirrors device agreed to in the Blair House Accords between the United States and the European Union that escaped the attention of most other countries. Currently, the EU and Norway constitute the main users of blue box policies. Some countries – including the United States – have advocated terminating the blue box, but there are no such payments to sugarcane or sugar beet farmers and the end of the blue box would have little impact on sugar trade.

All other trade-distorting support policies, other than blue box and green box policies and certain de minimis and special and differential policies, were gathered together into the Aggregate Measure of Support (AMS) and subject to reduction by 20% over 6 years, although with a credit for blue box subsidies and prior reductions. The United States ended up with large credits due to counting deficiency payments in the base AMS and taking credits for reductions in agricultural support in the 1985 and 1990 farm bills. In addition, the Freedom to Farm bill in 1996 moved a large part of the budget for agricultural subsidies from the amber box into the green box. In Europe, CAP reform in 1992 and since has moved a substantial share of the EU agricultural support expenditures from the amber box to the blue box in the form of blue box payments to wheat and cereals farmers.

As a result, neither the United States nor the European Union has been required to reduce anything. The U.S. price support program for sugar beets and sugarcane has continued at basically the same loan rates as have prevailed since the 1985 farm bill, and the EU sugar regime has not faced any significant reform.

In the next talks if there is an agreement for further domestic support reductions, it will likely be in a similarly modest scope due to the policies and politics of the European Union, Japan, Korea and some other like-minded countries. Another 20% or 30% cut in the AMS would still leave the United States with a large credit and would not require any change to the sugar price support program.

Under the no deal scenario, the status quo would prevail until the expiration of the peace clause in 2003. The peace clause provided a 9-year exemption from the Subsidies Agreement for domestic support measures that were in compliance with reduction commitments and that did not grant support to a specific commodity in excess of the support provided in the 1992 marketing year. The Subsidies Agreement makes domestic subsidies subject to challenge under WTO dispute settlement procedures if they cause injury to the domestic industry of another Member, or nullify or impair tariff concessions, or cause serious prejudice to the interests of another Member. Serious prejudice is deemed to exist if there is debt forgiveness (such as would happen upon loan defaults and collateral forfeitures) or subsidies to cover operating losses or if the total ad valorem subsidization of a product exceeds 5 percent.

The definition of a subsidy in the Subsidies Agreement includes any form of price support that confer a benefit. This would include the U.S. price support for sugarcane and sugar beets and could result in a challenge on the basis that it does allow for debt forgiveness in the event of forfeitures and does provide support in excess of 5% ad valorem if the difference between world prices and domestic loan rates are compared. Thus, the failure to reach an agreement in the upcoming agriculture talks could result in a much more significant challenge to the sugar price support program than if an agreement is reached to commit to further reductions of the AMS. The EU sugar regime and many other countries' sugar policies could also face WTO challenges under the Subsidies Agreement.

Next, let's take a peek at market access. In the Uruguay Round all non-tariff barriers to imported agricultural products were converted to tariff equivalents and all tariffs were bound and subject to reduction. Developed countries committed to reducing the tariff average by 36% and each tariff line by at least 15% over 6 years. Developing countries agreed to 24% reductions of tariff averages and 10%

minimum cuts over 10 years. "Current access" commitments required that market access could not be reduced from the quantities imported in the 1986 to 1988 base period, and minimum access commitments required developed countries to allow imports equal to at least 5% of domestic consumption by the end of the 6-year transition period.

What happened to sugar under the U.S. commitments on market access is difficult to explain. The U.S. had previously tariffied its absolute quota in 1990 with an unbound over-quota tariff rate of 16¢ per pound and no minimum quantity. In the Uruguay Round, the U.S. "re-tariffied" its former absolute quota (which had been found to violate the GATT by a dispute settlement panel) and achieved an 18¢ over-quota tariff which when fully reduced will be 15 1/3¢ per pound. This translates to a cut of less than 4% of the pre-existing rate of duty. The U.S. also accepted a current access commitment of approximately 1.25 short million tons, representing the average of imports during the 1986-1988 base period.

Will this exceptional result be possible again? Not likely. Many countries are calling for targeting tariff peaks, or tariffs over 20% ad valorem, for drastic reduction and demanding an end to the special agriculture safeguards. The tariff-quota rates are now bound and further reductions would be likely to be in the 20 to 40% range from the bound rates, if an agreement can be reached in this new round. This would leave an over-quota rate of about 12 1/4¢ to 9.2¢ coupled with a special safeguard triggered by prices or quantities. Considering transportation costs, a 20% reduction could still protect a 22¢ domestic raw sugar price whenever the world price was about 8 1/4¢ or more or an 18 3/4¢ price with world raws selling at 5¢ per pound.

Under the no-deal scenario, there would be no further reduction in the MFN tariff rate and the special safeguard would remain in place. This would mean no increase in imports from countries not parties to free trade agreements. Under this scenario, the domestic sugar industry would clearly benefit from the failure to conclude an agriculture agreement under the new round of trade talks.

Finally, let's take a look at export subsidies. In the Uruguay Round, the parties generally agreed to reduce export subsidies by 21% in terms of the quantities of subsidized exports and 36% in terms of the budgetary outlays. A flexibility provision allowed catching up in later years if subsidies exceeded the commitments. Since the round ended, a WTO dispute settlement panel and the WTO Appellate Body have ruled in the Canadian dairy case that a governmental regime for providing milk for producing exported dairy products at prices below domestic market prices constitutes a export subsidy payment subject to reduction commitments.

The United States has not yet provided explicit export subsidies for sugar and has a WTO commitment not to begin subsidizing sugar exports. The European Union uses export restitutions for B-quota sugar and C sugar is priced to be exported without explicit export restitutions. The EU commitment for 2000 marketing year limits subsidized exports to slightly under 500,000 metric tons However, the EU claims that it is entitled to deduct the quantity of imported sugar from its subsidized exports, deriving a "net export" figure, but the claim may not be justified under WTO agreements and precedents. Nonetheless, the EU has had to also claim a "rollover" of "credits" for unused export subsidies in 1995 and 1996 under the flexibility provisions even though the flexibility was not intended to allow such a rollover. Moreover, EU exports of C-sugar which don't qualify for restitution payments could be considered subsidized under the precedent established by the WTO panel in the Canadian dairy case, which has strong resemblances to the EU sugar regime. This would make exports of more than 5 million metric tons of B and C sugar subject to challenge under current WTO disciplines.

If the current negotiations reach a successful resolution on the Uruguay Round pattern, the European Union will have to make further cuts in subsidized sugar exports. If there is no agreement and the peace clause expires, the EU sugar export subsidies will fall under the Subsidies Agreement's total ban on export subsidies by 2003. That could force a major overhaul of the EU sugar regime. Under either scenario, the world market should be tighter and sugar prices should rise.

What indications are there that will be a deal or not? Firstly, trade negotiations on agriculture have usually been a battle between the United States and Europe. In the last round, the Cairns Group of exporting countries – Australia, Canada, Brazil, Argentina, New Zealand, South Africa, Mexico, Thailand, the Philippines, Hungary, Columbia, Uruguay, Indonesia, Malaysia, Paraguay, and Fiji – generally supported the United States for moving toward free trade of agricultural products. Japan, Korea, and the EFTA countries (Sweden, Norway, Austria, Switzerland, and Finland) generally supported the European Union in resisting any substantial reforms. These alliances are likely to continue. In addition, China will accede to the WTO and can be expected to resist any demands for more access to its market after having made major concessions in the accession negotiations.

Moreover, it is widely believed by people who participated in the last round of agriculture negotiations that agriculture cannot stand on its own without forming part of a deal that includes other sectors of the economy. This is because each participant needs to sell a deal domestically as something beneficial. But it is very difficult to see how the European Union or Japan or Korea can sell a deal at home that just reforms agricultural policies. Such a deal would be opposed by politically powerful agriculture interests and would not be sufficiently supported by broader interests. Even the United States could face serious problems getting Congressional approval of a deal that only included agriculture.

What can we conclude from all of this? The U.S. sugar industry faces a real challenge in the new WTO talks if there is an agreement to significantly improve market access by targeting tariff peaks or eliminating special safeguards, but it may be helped by the EU, Japan, China and Korea and others in resisting such reforms. On the other hand, if there is no new agreement, the sugar industry could face a challenge to the price support program under the provisions of the Subsidies Agreement after the peace clause expires. Under either scenario, domestic growers and processors must closely monitor the trade talks and hope that there interests are taken into account.