THE GOOD, THE BAD AND THE PRAGMATIC: AGRICULTURAL NEGOTIATIONS IN THE URUGUAY ROUND

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This paper addresses negotiations under the General Agreement on Tariffs and Trade (GATT) during the late 1980s with emphasis on agricultural products (1,2).

THE NEED FOR AGRICULTURAL TRADE NEGOTIATIONS

Trading relations among traditional partners and allies were marked by increasing tension in the 1980s. World economic growth rates slowed markedly from those of the 1960s and 1970s. This sluggishness in the rate of growth was due to a complex set of factors, among them the economic downturn that derived in part from US deflationary policies begun in the late 1970s, the serious debt situation in many developing countries, the strong US dollar and a sustained period of good weather in many countries. The United States felt the pinch acutely in the early part of the 1980s as imports rose and exports fell.

Although the current US trade deficit arises more from macroeconomic and physical conditions, many US industries and sectors blame subsidized foreign products and heavily protected foreign markets for their plight. They have been increasingly vocal in their calls for protection of US industries and for retribution against the "unfair trading practices" of other countries. US policymakers have begun to respond. The Omnibus Trade Bill, vetoed in 1988 by President Ronald W. Reagan, expressed much of this sentiment, and many of the trade provisions remain in replacement bills.

The United States is not alone in looking for ways to protect its producers, processors, and manufacturers. Many countries have increased the level of protection for their domestic industries, often using barriers that are not legal under the General Agreement on Tariffs and Trade (GATT). The resulting problems among world trading partners often threaten to escalate into retaliations and countermeasures characteristic of a trade war.

Agricultural trade mirrors, and in some cases magnifies, many of the tensions that are apparent in trade in general. The rate of growth of crop production outside the United States lagged consumption in the 1970s, giving US exports a tremendous boost. In the 1980s the relationship has reversed, with growth in crop production largely outstripping consumption. Trade has declined, with the rate of growth in world crop exports actually averaging minus one percent between 1980 and 1985. Agricultural trade disputes have also risen in the 1980s.

Trade in agricultural products does, however, differ in one major way from other trade in that a large part of it is excluded from many of the GATT rules and guidelines. In previous GATT rounds agriculture has been largely excepted, because most of the barriers to agricultural trade are not tariffs but stem from the domestic policies designed to support and protect the agricultural sectors in most developed countries. These domestic support programs frequently require border measures, such as quotas and variable import duties, to ensure that imported agricultural products do not undercut the domestically produced commodities supported by the programs.

The cost of agricultural support programs rose rapidly during the 1980s. From 1979 to 1981, the total yearly cost to consumers and taxpayers of agricultural subsidies in the industrial countries as estimated by the Organization for Economic Cooperation and Development (OECD) was about $100 billion. For 1984-1986, the OECD estimated that these subsidies totaled almost $220 billion annually. And yet, despite the large outlays, farmers in many regions experienced serious financial stress during the 1980s.

Increasingly, it seems, much of the cost of domestic programs goes towards offsetting other countries' agricultural policies. Support programs that raise domestic prices for agricultural products tend to decrease consumption and at the same time provide strong incentives to increase production. The resulting surplus production frequently moves into export markets, depressing world commodity prices. Lower world prices, in turn, often lead to higher levels of domestic support to maintain farm incomes at some politically acceptable level. As Figure 1 shows, about two thirds of the benefits to US producers from the support programs in 1986 were to compensate for the policies of other developed countries (International Agricultural Trade Consortium, 1988).

One of the most promising developments in agricultural trade during the 1980s was the decision to include agricultural trade more explicitly and more completely in the provisions of the General Agreement. The

United States led the charge, putting forward in July, 1987, a bold proposal suggesting dramatic changes in the domestic agricultural support policies of the industrial countries. The other major agricultural trading member countries responded with their own proposals. Unfortunately, the three main protagonists, the United States, the EC and Japan, took rather dissimilar stands and then stuck to their initial positions through most of 1988, making further progress difficult.

The midterm review of the Uruguay Round, held in Montreal, Canada in December, 1988, should have been a time for reviewing and reassessing positions and for injecting a strong dose of pragmatism into the agricultural negotiations. The failure of the parties to reach an agreement on the wording of the ultimate goal of the negotiations resulted in the adjournment of the review process until April, 1989 (and hence a deferment of the decision to fish or cut bait).

FOCUSING ON AGRICULTURE IN THE URUGUAY ROUND

The current round of multilateral trade negotiations, the Uruguay Round, began in September 1986, with a meeting of trade ministers from GATT signatory nations in Punta del Este, Uruguay. Agriculture's high priority in this round was noted in the communique issued at the meeting. It stated that the ministers agreed to "bring all measures affecting import access and export competition under strengthened and operationally effective GATT rules and disciplines" by _inter alia_ "the reduction of import barriers (and) by increasing discipline on the use of all direct and indirect subsidies, and other measures affecting directly or indirectly agricultural trade, including the phased reduction of their negative effects, and dealing with their cause" (GATT, 1986).

The rising cost of agricultural support programs and the increasing trade tensions among the major agricultural exporters, particularly the United States and the European Community were the key factors precipitating the focus on agriculture in the GATT. Also contributing to agriculture's high priority were the adverse effects of US/EC disputes on other exporters and the barriers to access to developed country markets for tropical products--especially sugar--from developing countries. Work done by the OECD on quantifying the extent of support and trade distortions pointed clearly at domestic agricultural policies in the industrial countries as being among the root causes of the "agricultural trade mess" (OECD, 1987).

The USA Proposal

For the United States, the aim in the agricultural negotiations of the Uruguay Round is to liberalize agricultural trade. Some steps toward liberalizing that trade are encompassed by the four main elements in the US proposal tabled to the negotiating group on agriculture in 1987. The first was the complete elimination of all production-and trade-distorting subsidies over a ten-year period. The second was the elimination of all barriers to market access, also over a ten-year period. The third was the elimination of nontariff barrier aspects of sanitary and phytosanitary regulations through harmonization. And the final element was that an aggregate measure of support, such as the "producer subsidy equivalent," be used for measurement, with commitments for reduction to be made on the specific commodities and policy measures.

This proposal was tabled relatively early in the negotiations. By the end of 1987, the EC, the Cairns Group (3), Canada (independently of the Cairns Group), Japan, and the Nordic countries (4) had tabled proposals in response to the US proposal (5).

Areas of Concurrence and of Conflict Among the Proposals

There is some common ground, but also some areas of conflict among these initial proposals. All countries call for harmonizing and minimizing the trade-distorting effects of sanitary and phytosanitary regulations, although there are differences among countries as to what harmonization would entail. All proposals, except that from the Nordic countries, would allow some form of special and differential treatment for the developing countries. The Nordic countries do not address the issue explicitly, but would most likely be sympathetic to the special needs of developing nations. With the exception of Japan, all initial proposals suggest that some type of aggregate measure of support is necessary in, or at least would be helpful to, the negotiating process. More recently, Japan has indicated that it would examine the relative merits of alternative aggregate measures of support.

The conflicts among the proposals are greatest on the issue of the degree to which subsidies and trade barriers will be reduced and the timing of any reductions. The United States initially focused on the long term goal of complete elimination of trade-distorting subsidies. The EC, Japan and the Nordics all want to retain some domestic subsidies, and the EC is interested primarily in relief from the current pressures on grain, dairy and sugar markets in the short term. The Cairns Group has a long term goal of eliminating all trade-distorting policies, but also sees the need for immediate relief measures. In July 1988, the Group submitted a proposal for a framework approach that would combine short- and long-term elements and begin reducing output-based agricultural support and liberalizing agricultural trade in 1989. The United States has shown some interest in the proposal and some willingness to be more flexible in considering short-term measures as intermediate steps leading to its long term goals (Lachia, 1988).

IMPLICATIONS OF THE US PROPOSAL (6)

The US proposal advocates the elimination of all trade- and production-distorting agricultural subsidies by the year 2000. If accepted, farm income could then be supported only by payments that are independent of the current and future level of a farmer's production and marketing, input use or commodity prices. Such payments are referred to as decoupled payments. The main economic arguments underlying decoupling, as defined in the US proposal, are that it would lead to an increase in the efficiency of resource use, while enabling the social goals of supporting agriculture to be met.

General Economic Impacts of USA Proposal

Decoupling would increase economic efficiency in two ways. First, removal of target prices would push farmers to make planting decisions based on prices that reflected the world supply of and demand for agricultural commodities (7). The burdensome surpluses of recent years would be reduced and eventually eliminated.

Second, removal of the acreage reduction programs would allow farmers to choose the most efficient combination of inputs. This shift in input mix, combined with changes in area planted, would reduce average costs of production, which in addition to benefiting domestic consumers would lead to greater competitiveness on international markets. The resultant increase in efficiency would free resources to be used elsewhere in the economy, increase exports, and lead to an increase in the rate of overall economic growth.

The US proposal seeks multilateral decoupling of farm support payments for all GATT member countries. Studies conducted by the OECD, the Economic Research Service of the US Department of Agriculture, and the World Bank indicate that multilateral decoupling would raise world commodity prices (OECD, 1987; Roningen et al. 1987; Tyers and Anderson, 1986). World price increases would be the greatest for commodities that now are highly protected, such as dairy and sugar, much less for grains, and virtually nonexistant for oilseeds. Trade would increase the most for rice, sugar and meat products (Roningen, et al. 1987).

Economic Impacts for the United States

The studies show different results for the United States. Roningen et al. report that multilateral trade liberalization would increase US exports of meat and meat products especially, but with smaller increases seen for US feed grain exports (1987). Robinson et al. show US grain exports and imports increasing and dairy and meat products exports decreasing and imports increasing (1988). Consumer prices for dairy products and sugar should fall, while consumer prices for other nonmeat commodities would likely rise. Producers of nonprogram crops such as fruits, vegetables and livestock, would face greater competition from former producers of program crops, but some might benefit from increased trade opportunities. Their net income position is unclear.

At the general economy level, these studies indicate the gross national product (GNP) would rise, the balance of payments would improve and the federal deficit would fall. It should be noted that these studies do not examine effects of the decoupled transfer payments on the budget or on farm income.

Although the United States has stressed its commitment to multilateral decoupling, some observers have suggested that, should such dramatic changes not be made world-wide, the United States should, nevertheless, go ahead and decouple on its own. Uncertainty about the domestic and trade policies of the US's competitors and trading partners make it difficult to predict the effects on US agriculture of unilateral decoupling. The size of the decoupled payments would be largely a political decision, which makes predictions of the effect on the budget difficult in both the unilateral and multilateral decoupling scenarios. Some studies of unilateral liberalization (not including the effects of decoupled payments) generally show improvement in the GNP and the budget deficit and a worsening in the balance of trade in the long run, resulting from decreased exports and increased imports of agricultural products (Hertel, et al. 1988). Highly protected commodities such as dairy, rice and sugar would experience the greatest decline in production in the long run. Production in the more competitive sectors such as food and feed grains would decline the least. Other observers, however, suggest that, at least in the short run, exports could increase as a result of eliminating acreage reduction programs and the consequent increase in production.

IMPLICATIONS FOR THE GATT NEGOTIATIONS OF THE NORTH AMERICAN DROUGHT

The drought that afflicted many regions of the United States and Canada in 1988 has changed the conditions for the negotiations in several ways. The large stocks that had a price depressing effect on domestic and world markets were drawn down during the year and not rebuilt with the 1988 harvest. Higher commodity prices and tightened supplies for US grains provide some relief for the EC because export restitutions decline when world prices rise. As the budget cost to the EC of continuing to subsidize agricultural exports has been one of the key pressures that has kept the EC in the agricultural negotiations, a reduction in this pressure could weaken their resolve and thus threaten progress in the Uruguay Round. Presumably it was this potential lessening of pressure due to the drought, together with a concern for the USA's reputation as a reliable supplier, that led the USA Administration to continue to use the Export Enhancement Program (EEP) throughout the summer, in spite of forecasts of much reduced production.

On the other hand, the increase in commodity prices caused by the drought also offers a golden opportunity for countries to freeze their levels of support at the new, drought-induced, lower level and thus make a real step towards reducing agricultural subsidies.

The 1988 drought also raised a flicker of concern among food importing countries that have become accustomed to buying agricultural commodities at bargain prices as the exporting giants waged subsidy wars in the world market. How would they fare if the vast stocks were to be reduced or eliminated and there were to be another year, or two, of serious drought in the grain producing areas?

A MORE PRAGMATIC APPROACH FOR THE UNITED STATES

The United States has proposed, and largely held to for the past fifteen months, the idea of the "zero option," which entails complete elimination of all trade-distorting agricultural subsidies by the year 2000. It should be noted, however, that US legislation was passed in 1988 that institutes new subsidies (for example, expansion of the EEP, the Farm Credit System bailout). Continued adherence to the concept of the zero option by the United States, and the EC's continuing resistance to it, have presented stumbling blocks for the rest of the negotiations. The important thing now is to move on, to indicate a willingness to discuss realistic, achievable goals and solutions for achieving them. The Uruguay Round has just passed its midpoint. Although the midterm review did not provide a clear framework and direction for the remaining two years of the Round, as had been hoped, the session should not be considered to have been a complete failure. Key issues were isolated and confronted and must now be addressed and dealt with by the major trading partners in the April review. It is imperative that some discernible progress be made in this round so the direction and point of departure is established for the next round of negotiations.

The United States, in the interest of achieving something of its bold objective, must be prepared to compromise (as, of course, must other nations) in some parts of its proposal. An article in "The Economist" called on the United States not to sacrifice possible gains in the short term--such as some (though less-than-total) reduction in subsidies and a move towards more liberal trade in agricultural products--for the possibly unachievable long term goal of complete elimination of trade-distorting agricultural subsidies. The US's proposed goal of achieving the zero option in just over a decade is unrealistic for the EC and Japan for several reasons. Much of the support for European and Japanese farmers is financed by consumers through higher food prices, in contrast to the USA system where taxpayers bear much of the burden. For the EC and Japan to phase out market distortions while still maintaining farm incomes at roughly their current levels would put an intolerable load on their budgets. An alternative would be to raise income tax rates to cover the higher cost, leaving society in general no worse off while improving the lot of the poor. The problem is, however, that raising taxes is generally viewed as a politically unpalatable. Second, and as importantly, in Europe and Japan agricultural support policies have strong historical, social and cultural roots, drawing on concerns about food security and the role of farmers in the society.

The United States also needs to pay attention to the home front. To date, relatively few US farm and commodity groups have made public their reactions to the US proposal. In part, their silence seems to stem from a belief that the proposal has little chance of being accepted in its current form and that they have nothing to gain from formulating and publicizing a position on it. The US Congress also has been quiet on the subject. It is unlikely, however, that either the Congress or the farm groups would rally to the support of the initial US proposal, even with assurance that other countries were prepared to open their markets to US agricultural products and reduce their agricultural subsidies. Many farm groups are suspicious of the idea of payments that are not tied to current production levels. A more pragmatic approach by the United States may be more likely to elicit the necessary support from both the farm groups and the Congress than will an unrealistic option that does not have clearly discernible benefits for the US agricultural sector as a whole.

CONCLUSION: AN OPPORTUNITY TOO GREAT TO LOSE

For many years the tangled web of domestic agricultural support programs has precluded any real headway being made to draw agriculture into GATT negotiations. In 1986, the major agricultural trading members of the GATT took the bull by the horns and announced that they would address agricultural trade and the trade-distorting effects of domestic policies and make agricultural trade liberalization a high priority goal of the Uruguay Round. The early positions taken by the chief adversaries in agricultural trade conflicts were, perhaps predictably, extreme and somewhat unrealistic. It is now time to get on with the business of negotiating, which means making concessions and compromising in return for achieving agreement on those issues most important to the parties involved.

At least one group has called on the United States and the EC particularly to resolve their differences and to work towards alleviating the trade-distorting effects of domestic agricultural policies. The International Policy Council on Agriculture and Trade recently issued a communique that called for an immediate freeze of production-linked supports and export subsidies, with agreement to reduce them further over the next two years (IPCAT, 1988). Over the longer term, the Council suggested that countries commit to an across-the-board cut in agricultural production subsidies of something less than 100 percent (they suggested at least 50 percent) over a set period, and that countries should begin to increase access to their markets and supplies of agricultural products.

Other observers have called more generally for liberalization of agricultural trade. "Mutual Disarmament in World Agriculture: A Declaration on Agricultural Trade" concludes that reforming agricultural and trade policies will lead to greater global economic efficiency and prosperity, a more sustainable environment, and greater global political stability (National Center for Food and Agricultural Policy, 1988). "Reforming World Agricultural Trade" points to the opportunity that GATT member nations have in the Uruguay Round to achieve significant reform of agricultural and food policies and the evidence that such reform will put farmers the world over on sounder economic ground and bring long term benefits to the global economy (Institute for International Economics, 1988).

In the negotiations so far the general thrust of these calls has been more important than the details. For the year following the tabling of the US proposal, countries stuck to the positions put forward in their initial proposals and showed little inclination to take even a small step towards finding common ground. The Cairns Group proposal of July 1988, was a first move towards a mutually acceptable compromise and that the United States has recently indicated some interest in the proposal is a promising development. It is now time to take advantage of this momentum. The time left in the Uruguay Round is too short to be spent dwelling on the relative merits of ideological but unrealistic options.

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NOTES

1. The views expressed in this paper are those of the authors and should not be taken as the official position of either the National Center for Food and Agricultural Policy or Resources for the Future.

2. Much of the background material on the GATT and the current negotiations is drawn from Agriculture in the Uruguay Round of the GATT, a briefing book issued by the National Center for Food and Agricultural Policy (Washington, D.C., Resources for the Future, August, 1988).

3. The Cairns Group includes Argentina, Australia, Brazil, Canada, Chile, Colombia, Hungary, Indonesia, Malaysia, New Zealand, Philippines, Thailand, and Uruguay. Fiji is also a member of the Cairns Group, but did not sign the proposal to the GATT. The Group is named after the Australian city in which it first met in 1986.

4. The Nordic countries are Finland, Iceland, Norway, and Sweden.

5. For more detail on the other proposals, see Agriculture in the Uruguay Round of the GATT, see note 2.

6. This section is drawn from Agriculture in the Uruguay Round of the GATT, see note 2. See also, Decoupling Farm Programs, a briefing book issued by the National Center for Food and Agricultural Policy (Washington, D.C., Resources for the Future, April, 1988).

7. Target prices are legislatively set prices for wheat, feedgrains, rice and cotton that are determined to be the minimum required to provide a "fair return" to farmers. The target price is used to determine the size of the direct (deficiency) payment that producers of these program crops receive from the government; this payment is calculated as the difference between the target price and the higher of the market price and the loan rate for each of the crops.

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