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## Obstacles to progress in multilateral agricultural trade negotiations: Accommodating the needs of developing & transition countries

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# OBSTACLES TO PROGRESS IN MULTILATERAL AGRICULTURAL TRADE NEGOTIATIONS:

Accommodating the Needs of  
Developing & Transition Countries

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Don McClatchy

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NZ Trade Consortium Working Paper No. 9

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## Abstract

*Although the WTO Agreement contained many provisions for 'special and differential' treatment, it is now generally accepted that developing countries have yet received rather few real benefits from the Uruguay Round. The hunt is on to find ways to better address the needs of these countries in the new Round; some suggest the credibility and viability of the WTO itself is at stake. Several suggestions already exist about what further might be done. This paper proposes an additional step which might be taken in the agricultural field.*

*Developing and transitional country governments have a need to protect their farmers (and, often, consumers) against external shocks, particular arising from world market price swings. Typically lacking fiscal resources, their only feasible approach to do this may be through the use of border measures to moderate price transmission to the domestic market. With non-tariff barriers and export subsidies now effectively removed from the choice set for most, what remains are variable tariffs, variable import subsidies and variable export taxes (and, to a limited extent, controls on export quantities).*

*Many developing countries emerged from the Uruguay Round with bound tariffs quite high relative to applied tariffs. This gives them considerable 'room' to vary the applied tariff as a domestic price stabilising measure. Some have formal policies in place to do so systematically. Others have done it on a more ad hoc basis. However, questions have been raised about the WTO-legality of such practices because the Agreement on Agriculture explicitly bans some types of variable tariffs ('variable import levies' and 'minimum import prices'). The reality is that such 'banned' schemes are still in operation in the EU and Japan, and some other existing forms of variable tariffs (e.g., 'seasonal' tariffs) have not been challenged, and appear to be widely acceptable.*

*It is concluded that clarification is needed about which types of variable tariff practices are to be allowed and which are not. Rather than opposing developing countries' use of 'sliding scale' tariff schemes and lamenting their high levels of tariff bindings, the OECD group could recognise these countries needs, not exaggerate the costs to themselves, and endorse the practice of varying the applied tariff as a stabilising measure for import-competing agricultural producers and for consumers of the same commodities. As a 'special and differential' concession, developing and transition countries could be allowed to retain tariff bindings at a level high enough to provide a capacity for using variable tariffs as a safety net measure. Conditions and incentives could be attached to ensure transparency, predictability, and a principally stabilising (not permanently protective) tariff use. Any new disciplines on export taxes or controls should take into consideration the logical linkage and be made consistent with such a concession.*

## 1. INTRODUCTION

This paper sets out to do two things. The first is to provide a brief review, both in general and more specifically agricultural terms, of the current situation in the World Trade Organisation (WTO) and multilateral trade negotiations (MTNs) from the perspective of developing countries (DCs) and transition countries (TCs). The second is to build a case for a 'special and differential' (S&D) concession which could be made to DCs and TCs in the agricultural market access area to increase their perceived benefits from MTN participation and thus contribute to progress in the negotiations newly underway. To some extent, these two tasks are pursued simultaneously.

Section 2 provides some general background to the S&D treatment DCs have received in the GATT and WTO agreements and summarises the 'big picture' at the present time (early 2000) concerning the role these countries are likely to play in the new negotiations. It emphasises the growing relative importance of the DC/TC bloc in the WTO, and reviews the main reasons for many of these countries' current discontent and the various solutions which have been proposed to address their concerns, both generally and in the agricultural area.

The third section of the paper re-examines the Uruguay Round Agreement on Agriculture (URAA). It summarises the range of instruments historically used to support and stabilise farm incomes in developed countries (hereafter 'OECDs') and the general logic underlying the agricultural trade and domestic policy disciplines agreed in the URAA. It goes on to compare the typical patterns of agricultural support in, and WTO commitments faced by, DCs and TCs, respectively, and to review the deficiencies of the URAA disciplines and modalities in application to DCs and TCs. One particular shortcoming is singled out for its importance and for attention in the remainder of the paper, - the lack of practicable access for DCs and TCs to a farm price or income stabilisation tool under the existing URAA disciplines, if these are interpreted as excluding the ability to periodically vary applied tariff levels.

Section 4 focuses on this particular issue of the use of variable tariffs as a domestic price stabilisation measure. An attempt is made to summarise the different types of such schemes which have existed or still do, the treatment of variable tariffs generally in the Uruguay Round (UR), and the post-UR situation.

Section 5 includes some suggestions about how a clarified WTO discipline incorporating an explicit S&D concession for DCs/TCs could work, and discusses its potential advantages and disadvantages from both DC/TC and OECD perspectives. The conclusions of the paper are summarised in section 6.

## 2. BACKGROUND AND OVERVIEW

### Special and Differential Treatment

The principle of S&D treatment for DCs was adopted in the Tokyo Round of MTNs in the 1970s (Winham, 1986) though the concept of differential provisions for such countries had appeared as early as 1948 in the ill-fated Havana Charter (Josling et al, 1996). S&D continues as one of the philosophical underpinnings of the WTO. In the URAA, for example, this principle was reflected in the preamble which refers to an agreement that OECDs would provide “a greater improvement of opportunities and terms of access for agricultural products of particular interest to these countries, including ..... tropical agricultural products.....”. Other specific URAA S&D provisions included allowing DCs a longer implementation period for their commitments (10 years rather than 6), and to face smaller percentage cuts in their base period tariff levels, export subsidies, and non-exempt domestic support (AMS) levels. Additionally, DCs alone were formally given the option of nominating “ceiling bindings” on tariff rates in their schedules, rather than binding their tariffs at or close to base period applied levels. The URAA exempted, for DCs only, certain types of programs from being counted for export subsidy (Article 9.4) and AMS (Article 6.2) reduction purposes, respectively, and AMS ‘de minimis’

levels were higher for DCs. Furthermore, a distinction was made between least developed countries (hereafter LDCs) and other DCs, with the former being granted more lenient commitments in some respects. Other Uruguay Round (UR) agreements incorporated their own specific S&D provisions.

### Current concerns

Now, six years later, with DCs accounting for an ever-growing majority (now over 100, or about 75%) of WTO members, and for a recently growing share of total world goods exports (now approaching 30%), we witness an important and seemingly still-growing concern that -

- a) LDCs have obtained rather few benefits from the UR, particularly in terms of improved access to developed country (hereafter OECD) markets for products of interest to them, like sugar, tobacco, peanuts, cotton, processed fruits and vegetables, and textiles<sup>1</sup>. A number of factors have been blamed for this, in particular:
  - negligible increases in OECD import quotas (e.g., for sugar), the common allocation of these quotas on a country-specific ('non-MFN') basis, and prohibitively-high over-quota tariffs for many sensitive agricultural products (such tariffs, because of the 'water' they contain, may have to be reduced considerably before an economic incentive for over-quota trade is created);
  - negligible progress in reducing the incidence of tariff escalation in OECDs, particular insofar as it affects the location of processing of raw products of DC origin;
  - delayed introduction of new OECD import quotas under the UR Agreement on Textiles and Clothing;
  - erosion of existing DC tariff preferences (under the Generalised System of Preferences (GSP), the Lome Convention, the Caribbean Initiative, etc.) as 'most favoured nation' (MFN) tariffs are reduced by OECD countries<sup>2</sup>;

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<sup>1</sup> While OECDs' MFN tariffs on raw tropical products were in general reduced in the UR, and are now quite low, even lower preferential tariffs, not the subject of UR reductions, are often the operative tariffs facing such countries exports to OECD countries. Furthermore, operative OECD tariffs on processed tropical agricultural products (whether MFN or preferential) are typically much higher (escalation).

<sup>2</sup> For example, Yamazaki (1996) estimated the value of losses, just of preferences granted by the EU, the US and Japan in the agricultural field alone, to be \$0.7 billion per year. Tangermann & Josling (1999) estimated

- failure of many DCs to take full advantage of the new trade opportunities opened up to them.
  
- b) DCs took on commitments in the UR which were unrealistic for them in terms of time requirements, human capital requirements and fiscal costs of implementation, in particular with respect to:
  - reforming trade procedures, like import licensing and customs valuation;
  - reforming many areas of regulation, such as technical standards, sanitary and phytosanitary standards, and intellectual property<sup>3</sup>;
  - the broader infrastructure capacity (transportation, port, communications, information, education, etc.) investments needed in order to be able to take advantage of the new trade opportunities.
  
- c) DCs are still not able to participate effectively in the WTO machinery or get their voice heard in negotiations, for reasons such as:
  - the fiscal costs of maintaining representation and servicing meetings in Geneva, their lack of suitably trained and experienced people, and poorly developed communications between foreign posts and capital offices and between ministries<sup>4</sup>;
  - their exclusion from traditional WTO ‘green room’ and ‘informal’ meetings where key decisions are taken (an internal transparency problem);
  - their relatively small individual size, particularly when measured in terms of share of total trade, and the difficulties of forming negotiating ‘blocs’ or ‘coalitions’ where the various partners can agree on a common position, in order to strengthen their collective negotiating leverage;
  - their influence in discussions about trade rules is compromised by their position as recipients of ‘S&D’ treatment.<sup>5</sup>

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that the value of preference margins for ACP exports to the EU under the Lome Convention, estimated at over 600 million ECU for ‘non-protocol’ agricultural products plus beef and sugar, could be eroded by 60-70% due to MFN tariff cuts in a new MTN Round which were similar in magnitude to those achieved in the Uruguay Round.

<sup>3</sup> Finger & Schuler (2000) discuss this general problem at some length and argue that the cost for a LDC to implement its WTO obligations in just three of the six UR Agreements which involve the restructuring of domestic regulations is in the order of \$130 million, - more than the total annual development budget for many such countries. They question whether “doing it the OECD way”, which is implicit in these obligations, is necessarily the best approach to DC reforms in these areas.

<sup>4</sup> See, for example, results of a study by the African Economic Research Consortium of sub-Saharan African countries’ participation in the rules-making exercises of the UR, cited in Finger & Schuler (2000). Presently, 28 WTO member countries do not have a permanent representative in Geneva.

<sup>5</sup> Because of this ‘price’ associated with S&D, Tangermann & Josling (1999) urge caution on the part of DCs. Rather than seeking broader use of the concept, they suggest that it may be in the interests of these



## Responses to these concerns

The above concerns also apply in large measure to countries which prefer to class themselves as ‘transition’ rather than ‘developing’ countries (and to countries in either group which may have joined the WTO since 1994 or be still in the process of accession)<sup>6</sup>. In the lead-up to the Seattle Ministerial meeting in November 1999, and subsequently, they have generated various responses, such as:

### i) Responses from within the trade establishment:

- Rhetoric: Increased formal recognition, in communiques, speeches, etc., of the need for the international community to provide more help to LDCs and small economies to participate in the multilateral trading system. Many see this as a necessary condition for the continued credibility and viability of the WTO. There was a proposal to call the next round of multilateral trade negotiations the “Development Round”.
- Action: New and expanded technical assistance initiatives from the WTO, the World Bank, UNCTAD, the FAO, other organisations, the EU, and some individual countries aimed at increasing the capacity of DCs and transition countries (hereafter TCs) to understand the WTO texts and process and to participate effectively in the organisation;

### ii) Responses from DCs themselves;

- A general lack of enthusiasm for a new multilateral trade negotiation (MTN) round, and a preference that it be postponed, at least with respect to anything beyond the ‘built-in agenda’ already mandated by the 1994 WTO Agreement;
- Suggestions that the immediate priority should be for the OECDs to implement more fully their existing UR commitments, for some revisions and

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countries to seek to confine S&D to “a small set of trade policy areas where DCs have particular difficulties”.

<sup>6</sup> For the purposes of this paper I exclude from the category “transition countries” those Eastern European countries which are already accepted in principle for future EU membership, and whose goals, level of development and fiscal situation sets them distinctly apart from most other former soviet bloc countries. I would also exclude from “DCs” relatively rich countries like Singapore, Hong Kong, Brunei, and S. Korea.

clarifications to certain UR agreements (e.g. TRIPS)<sup>7</sup>, and for a revision of some DC implementation periods to make them more realistic.

- Strong opposition to proposals from within the OECD group to expand the scope of the WTO to include such things as labour standards, environmental standards, competition policy, and expansion of the rudimentary UR Agreement on Trade-Related Investment Measures (TRIMS)<sup>8</sup>. These are perceived by many DCs as no more than disguised new avenues for OECD protectionism.

iii) Concrete proposals for agenda items, approaches or modalities which could be adopted in the new round to address the concerns and aspirations of the DCs and correct the apparent imbalance in the distribution of benefits deriving from the UR. These have come from various sources, - academia, international institutions, non-government organisations (NGOs), member governments, etc., and range widely in nature. It is assumed that they would supplement, rather than substitute for, the more traditional S&D provisions, like smaller depths of cut and longer phase-in periods. Among the more general proposals to have been heard are the following:

- that the OECD group grant immediate tariff-free entry for all imports of goods from the LDC bloc;
- that existing DC tariff preferences be 'bound' (implying that any future reductions in MFN tariff rates would be accompanied by corresponding reductions in any preferential rates)<sup>9</sup>;
- that all cases of tariff escalation be eliminated;
- that certain OECD S&D commitments which are currently only of a 'best endeavours' or otherwise non-binding nature, be made binding;
- that DCs form negotiating coalitions, to ensure their representation at the table when the important decisions are taken<sup>10</sup>;

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<sup>7</sup> The suggestion by the chair of G77 in Sept. 1999 that the Seattle meeting should be a time to "review, repair, and reform" past agreements and implementation procedures, rather than expanding the WTO's agenda to new sectors, has been echoed by many DC spokespersons (Barry, 1999).

<sup>8</sup> This may to some extent be pre-negotiation posturing. Binswanger & Lutz (2000) argue that, while recent analysis by Anderson et al (2000) indicates that agriculture provides the most potential for DC gain in a new round, OECD concessions in this area will probably have to be justified by gains in other areas, which may not be possible if the scope of the negotiations is kept narrow. Broadening the agenda can provide all participants with more negotiating leverage.

<sup>9</sup> Clearly there is a limit to the extent to which preferences can be preserved in this way. After preferential tariff rates have been reduced to zero, then further negotiated reductions in MFN rates must, by definition, erode such preferences, unless preferential import subsidies were to be introduced (very unlikely).

<sup>10</sup> Personally, I see this as necessary, albeit fraught with difficulty. It appears that the major trade-offs in negotiations about rules are only possible with a few players at the table. In the UR, the Cairns Group was

There have also been some more specifically agricultural proposals, including:

- that there be early agreement to force down ‘tariff peaks’ (reduce tariff ‘dispersion’), such as exist in areas like rice, sugar, and dairy, through tariff-reduction approaches such as the use of a “Swiss formula”;
- that all TRQs be allocated on a strictly non-discriminatory basis (country reservations abolished);
- that rules for calculation of “Current Total AMS” be changed to give countries facing a “Total AMS” limit of zero (most DCs) the same between-product and product-specific/non-specific flexibility for allocating “non-exempt” support as is currently enjoyed by OECDs with significantly positive “Total AMS” limits<sup>11</sup>;
- that countries agree to significantly increase market access for all products of export-interest to DCs;

There is no attempt here to evaluate the above and other proposals. Individually, they probably all have some merit, though Tangermann and Josling (1999), in their comprehensive review of the interests of DCs in the next round of agricultural negotiations, point out the weak influence of S&D recipients in negotiations about rules from which they are released from some obligations, and make a persuasive case for DCs to be rather selective about the concessions they seek. In the agricultural area specifically, my view is that the ensemble of suggestions is still collectively insufficient<sup>12</sup>, in that they do not yet adequately address a key underlying problem. This argument is developed further in the remainder of the paper.

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able to develop common position papers in several areas, which made it a force to be listened to in the Agriculture and SPS discussions and probably helped many of its members to participate in the process long after they would otherwise have been excluded. However, the members of the Group still negotiated individually (unlike the EU countries), and so, despite collectively accounting for a bigger share of world agricultural product trade (exports + imports) than the US, the Group was excluded from the Blair House negotiations.

<sup>11</sup> There are several ways in which this could be done. The simplest may be to apply a single de minimis at the Total AMS level (20% for developing countries). At the same time, the current ambiguity about how to count negative product-specific AMS could be removed.

<sup>12</sup> This assertion is consistent with the failure of the Seattle meeting; LDC dissatisfaction with OECD country positions, - in particular that of the US, - was at least a contributing factor to this failure.

### 3. A RE-ASSESSMENT OF THE URAA CONSIDERING DC/TC INTERESTS

#### Synopsis of OECD farm income support

Farm income support has been arguably the most important element of OECD countries' agricultural policy packages in recent decades. It certainly has accounted for most of the public funds expended in this area. Typically, it is pursued with a combination of border and domestic measures, though either alone can be used. It is also typical that the types and extent of support provided by any given country differ among commodities, while being more likely to be similar for 'like' commodities (e.g., 'red meats', or 'cereal grains'), and while recent years have seen some moves towards 'whole farm' income support in some countries (e.g., Canada).

The term "support", when applied to farmers' incomes, typically has two connotations or elements: augmentation and stabilisation. In more cases than not, they are jointly pursued in actual support programs. Also, the immediate target of the support may be some definition of "income" (incorporating both price and quantity factors) or simply "price"<sup>13</sup>. If price is manipulated, it may be the "market price" (in which case consumers as well as producers will be affected by the measure) or the "effective price" to the producer. A simple classification of the policy target variables and corresponding instruments may thus be<sup>14</sup>:

- a) Market Price Augmentation: fixed import tariff<sup>15</sup>; fixed per-unit export subsidy.

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<sup>13</sup> There tends to be a loose presumption that, if price is made more stable, then income will also become more stable. Similarly, there is a presumption that compensations for yield variability, e.g. through crop insurance payments, will also reduce income variability. While the logical possibilities for an inverse correlation between price and aggregate supply, and a positive correlation between any given individual farmer's yield and aggregate supply are recognised, these presumptions are still thought to have at least partial validity at the individual farm level in an openly trading country, even a relatively big one.

<sup>14</sup> Other logical possibilities for which OECD examples are uncommon have been excluded here, as have effective price stabilisation or price reduction initiatives focused on consumer price levels, which have been common in DCs and TCs. In some cases combinations of the instruments listed will be necessary; i.e., they are not all 'stand-alone' options.

<sup>15</sup> In this paper I use the word "tariff" in a broad sense to include any and all border charges, whether fixed or variable, whether specific or ad valorem (percentage) or more complex, which are paid per unit of product imported. That is, I do not distinguish between "tariffs", "duties", "levies", "fees" and other border

- b) Effective Price Augmentation: fixed per unit output subsidy (direct payment).
- c) Income Augmentation: input subsidy (direct or indirect payment).
- d) Market Price Stabilisation and Augmentation: variable import tariff; variable export subsidy; import quotas; intervention purchases; old US loan scheme; asymmetric buffer stocks; supply controls.
- e) Effective Price Stabilisation and Augmentation: deficiency payments; new US loan scheme; price stabilisation programs.
- f) Income Stabilisation and Augmentation:<sup>16</sup> crop insurance; disaster payments; revenue stabilisation programs.

The term “stabilisation”, as used here, needs qualifying. It refers to government policy offsets or compensations for longer-term ‘swings’ in market prices or incomes, - changes with a duration in the 3-month to 3-year range, rather than in the 3-day to 3-week range. To a considerable degree farmers can use commercially-available risk instruments to protect themselves against the shorter-term price variability. While examples of legislated seasonal price-pooling schemes still exist, many governments prefer not to interfere in the shorter-term arbitraging of the market and or in farmers’ marketing decisions (witness, for example, the payment of former US deficiency payments based on seasonal average market prices, rather than on individual farmers’ returns).

It may be (cynically) argued that farmers ask for ‘stabilisation’ and ‘safety net’ programs simply because they realise that government handouts to farmers are more acceptable to the rest of society in low price years; i.e., that their sole real interest is in income augmentation. A test of whether farmers are genuinely interested in income stabilisation, as well as and as distinct from income augmentation, could be their enthusiasm for purely stabilising measures, - in which they would forego windfall gains in high price years as well as being compensated in low price years,

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charges, except those which are applied directly to the administrative cost of a trading service. My use of “tariff” thus corresponds to an economic effect, and not a semantic label.

<sup>16</sup> Programs are considered to be income ‘augmenting’ as well as ‘stabilising’ if net government contributions occur over time; i.e., if payments to farmers exceed premiums or other contributions received from farmers over, say, a decade or more.

- if offered no other option. Admittedly, examples of purely stabilising farm income support programs in OECD countries are rare (perhaps confined to a few past attempts to implement symmetric buffer stock schemes). It is possible also that governments build stabilising dimensions into their farm income augmentation efforts for broader economic reasons<sup>17</sup>. The debate about the real motivation for the existence of stabilising elements in farm income support programs goes beyond the scope of this paper. The important point is that OECD governments do perceive a great political need to transfer more income to farmers, one way or another, in years of low market prices<sup>18</sup>. This is empirically observable and undeniable. In the years 1998-2000, for example, the US government has found it necessary to top up by roughly \$10 billions per year the farm payments already mandated by the 1996 FAIR Act, in response to lower than average farm product prices. The Canadian Government, despite having an income safety-net program (NISA) already in place, has responded similarly over the same period, with additional annual payments in the rough order of C\$ 1 billion.

It can be noted that all the ‘market price’ options listed above (categories a) and d)) together correspond to what is often called “market price support” (MPS). Most of the remaining options fall into the general category “direct payment support”. All are recognised as being, to a greater or lesser extent, ‘coupled’ to production and trade-distorting, and it was the above group of measures which became the main targets for discipline in the UR negotiations on agriculture.

### The logic of the URAA disciplines

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<sup>17</sup> For example, some cropping farmers may be able to cope adequately with major year-to-year income variations by confining their new machinery purchases to their above-average income years. However, such behavior can, in aggregate, have serious repercussions for machinery manufacturers and dealers, and may lead to inefficiencies and higher machinery prices.

<sup>18</sup> We policy advisors have relied heavily to date on evaluations of the effects of trade and domestic policy instruments based on a ‘steady state’ assumption with regard to world markets. The reality is different. So, in addition to putting numbers on the **average** income transfers over time between different groups in society which various interventions generate, policy analysts should also be striving to measure the

It seems to me that there were three main arguments underlying efforts in the UR to craft undertakings and disciplines which would curtail the trade-distorting effects of farm income support programs. These corresponded, respectively, to concerns about effects of programs on the level of world market prices, effects on the stability of such prices, and effects which could not easily be discerned. For simplicity, I will refer to these here as the ‘static’, ‘dynamic’ and ‘transparency’ arguments, respectively. They gave rise to the following implicit working objectives, and disciplinary approaches:

i) Static arguments:

- Domestic market price support (augmentation), which has the effect of stimulating domestic production and depressing domestic consumption, and therefore of stimulating net exports and depressing world market price, is arguably the most serious form of trade distortion, and should be reduced as rapidly as possible. It is widely recognised that this form of support is dependent on the use of border measures (tariffs, import quotas, export subsidies, etc.) and could be effectively, albeit indirectly, controlled with disciplines on these measures alone. Tariff and export subsidy reduction commitments do appear to have caused some reduction in MPS levels in OECD countries over the past 6 years, but clearly much scope remains.
- Output-related direct payments to producers affect only the effective supply price, and thus only domestic production. Arguably, the stimulative effects of such programs on net exports and their depressive effects on world prices are more dilute. Also, they are fiscally more costly and therefore more likely to be kept in check by affordability considerations. Nevertheless, there was a strong consensus during the UR that they should also be the subject of limitation and reduction, which, given their independence of border measures, necessitated the addition of a separate discipline on domestic support (upper limits on the Aggregate Measure of

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economic value over time, recognised by politicians, of more stable effective prices for producers and consumers.

Support or AMS). It is still not clear, however, that any significant reduction in these types of programs has yet occurred because of countries' AMS constraints.

ii) Dynamic arguments:

- To the extent that a country uses instruments which buffer its producers (and/or consumers) from world market price fluctuations, then that country's supply (and, possibly, demand) response to such fluctuations is dampened or eliminated. Also, if domestic prices are not allowed to move up or down in response to domestic supply fluctuations (mainly year-to-year, weather-related yield variations), the magnitude of net trade of that country will show more variability over time. In both instances, the effect is to push more (or all) of the burden of adjustment on to the world market, - in effect, on to other countries, - and to cause world market prices to be more unstable than they would otherwise be. The phenomenon has been sometimes characterized as "exporting instability" and epitomized by the EU's use of its infamous 'variable import levies' (VILs). Such thinking led to the 'elimination' of 'non-tariff barriers' (NTBs) such as VILs, MIPs and quantitative restrictions (QRs) in the UR. However, the 'tariffication' of many of these NTBs led to the creation of tariff-rate quotas (TRQs) with high over-quota tariffs whose prohibitive level means that negligible transmission of world price changes to the domestic market continues in such cases. Furthermore, the EU has been able to retain, with only minor changes, its variable tariff mechanisms for cereal grains (including rice) and certain fresh fruits and vegetables. Thus, to a large extent, this problem remains.

iii) Transparency arguments:

- The multilateral trade establishment has long embraced the principle of 'transparency', which, in the context of import restrictions, tends to be interpreted as implying 'tariffs-only protection'. Such thinking naturally also gave support to the idea of tariffication of all agricultural NTBs in the UR. More generally, the concern



is with any sort of measure whose possible trade-distorting effects are very difficult or impossible to analyse. Thus, while the tariffication exercise was successful in eliminating some such measures, others appear to have slipped through this and other UR 'nets'. Transparency concerns remain about policy instruments such as US export credit programs, some food aid programs and the Canadian and Australian Wheat Boards, which are prompting calls for further clarifications and extensions of existing disciplines in the next round of MTNs.

### Reconciling farm income support goals and WTO disciplines

The specific URAA commitments and disciplines have been reviewed and summarised widely<sup>19</sup>, and by now are well known. While the policy adjustments required in OECD countries to remain in conformity with their obligations have so far been minimal, there is a general tacit acceptance that a long term 'reform process' has been established and that the reductions of the UR will be continued in further MTN rounds. If this happens, then, by extension, a time will ultimately be reached where all export subsidies and NTBs are eliminated, and bound tariffs are all zero. How will countries then be able to pursue their goals of farm income stabilisation?

The answer implicitly provided by the URAA is that then governments can continue to do so, free of international constraints, through the use of 'green box' measures; i.e., programs which satisfy the criteria of Annex 2. Such programs will have to be publicly-funded (not involve transfers from consumers), and not have the effect of providing price support to producers. To the extent that they involve direct payments to producers, the amount of payment must not be related to quantities of production or of inputs used, or be related to output prices, and individual "eligibility for payments must be determined by clearly-defined criteria such as income, status as a producer or landholder, factor use or production level in a defined and fixed

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<sup>19</sup> Unfamiliar readers are referred to IATRC (1994).

base period” (non-zero current production must not be required for eligibility)<sup>20</sup>. In short, such payments must be targeted.

While not precluding other or new types of programs which satisfy these general criteria, Annex 2 of the URAA sets out more specific criteria corresponding to selected particular program types. Thus paragraphs 7 and 8 refer to income insurance, income safety-net, crop insurance and disaster payment programs, all of which would serve the income stabilisation and income augmentation goals. Subsequent paragraphs of Annex 2 deal with payments to farmers which might be justified on other grounds, such as structural adjustment assistance (for farmer or resource retirement, or new farm investments), environmental stewardship, or disadvantaged region assistance. Some of these latter may be used partially to pursue farm income support goals on a more limited scale.

In summary, the URAA was perceived as leaving plenty of doors open for countries to pursue farm income augmentation and stabilisation goals in minimally-trade-distorting ways. Implicit in the URAA is a template (Annex 2, or the ‘green box’) of means to farm income support goals which are not significantly trade-distorting. But the green box was designed by OECD countries for OECD countries. The problem is that, because of the current circumstances (fiscal resources, infrastructure, etc.) in DCs and TCs, most green box options are not feasible alternatives for them.

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<sup>20</sup> URAA, Annex 2, Paragraph 6.

## Patterns of support in DCs and TCs

While considerable diversity exists, certain typical patterns are already well-documented and recognised<sup>21</sup>.

A major source of differences from the pattern in OECD countries derives from the relative historical importance, in DCs and TCs, of keeping urban food prices low. Food subsidies have thus been common in the past, making major demands on scarce fiscal resources, and exchange rate manipulation has also had serious consequences for farmers. As a result, many DCs have until recently taxed rather than subsidised their farmers in an average year (some still do). Neither direct support payments to farmers nor open market price support, which drives domestic prices above world market prices, have typically been very important in these countries. On the other hand, two-price schemes, with higher prices to farmers and lower prices to consumers translating into regular substantial losses born by marketing parastatals, have been quite common. Similarly, credit and input subsidies, provided indirectly through government transfers to the loss-making delivery institutions, have been the other main form of publicly-funded support to farmers, and have counted for a much higher percentage of total support than they do in the OECD countries<sup>22</sup>.

Stabilisation has occurred here too. Schiff and Valdes report that, in the 18 DCs studied in detail by the World Bank about 10 years ago, “domestic price stability” was one of four “primary objectives” of agricultural policy, that “most countries, responding to the instability of world markets, intervened to stabilise domestic producer prices relative to world prices”, and that “on the whole, direct price interventions have achieved the objective of stabilising domestic agricultural prices”. In DCs, stabilisation of producer incomes has been largely pursued via the controlled or supported prices for major farm outputs and inputs, with market price fluctuations giving rise to variable year to year parastatal losses.

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<sup>21</sup> See, in particular, Krueger, Schiff & Valdes (1992), - usefully summarised in Schiff & Valdes (1995).

An important feature to note about this pattern is that it does not involve any significant direct payment of cash subsidies to farmers in DCs and TCs. In fact, with large numbers of small producers, poor or non-existent records on individual farms, shortage of adequately trained administrative personnel, and other infrastructural deficiencies, such payments are in practical terms not currently feasible in most DCs. In TCs, the situation is somewhat different, and cash support payments to individual production units based on their farm records might be more feasible, though again have not been used much to date. Here the production units are typically large (ex-state farms, cooperatives, etc). As the private ('family') farm sector grows in importance in these countries, their situation will become more akin to that in DCs, and the use of direct support payments to individual farms increasingly impracticable.

As a result of the above typical pattern of base period support, and their recourse to somewhat different tariff binding and 'tariffication' modalities, many DCs now have export subsidies bound at zero levels<sup>23</sup>, no TRQs, bound tariffs well above applied tariff levels, and 'Total AMS' limits at zero<sup>24</sup>. The implication of the last of these is that 'non-product-specific, non-exempt' support (input subsidies) may be granted only up to 10% of the total value of agricultural output, and 'product-specific, non-exempt' support may be granted for each individual product only up to 10% of the value of that product.

Many TCs are relatively new WTO members or are still in the process of accession.

Consequently, their agricultural commitments have been (or will be) based on selected years in the decade of the 1990s; i.e., after the break-up of the Soviet Union, and during a period when many of the earlier Soviet-area subsidies had been withdrawn, production had fallen drastically, and these countries were in a net import position for most products. Given this situation, it is not

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<sup>22</sup> In some cases such input subsidies have been viewed as an offset to costs imposed on farmers by low product price maintenance policies.

<sup>23</sup> There are only 10 DCs with export subsidy reduction commitments.

<sup>24</sup> More than 90% of total notified 'base year' Total AMS was accounted for by OECDs; 61 of 71 DCs notified a base Total AMS of zero (implying de minimis levels of all product-specific AMSs and of non-product-specific AMS) (UNCTAD, 1999).

surprising that they too are tending to emerge from the process with AMS limits at low or de minimis levels, and with little or no scope for future use of export subsidies. Strong pressure appears to have been put on these countries during the accession process to bind their agricultural tariffs close to currently applied levels. Like DCs, few have TRQs.

#### Deficiencies of URAA modalities and disciplines in application to DCs and TCs

URAA modalities and disciplines were devised almost entirely by people from OECD countries with OECD types of support and protection in mind, so a degree of unsuitability for DC and TC situations is hardly surprising. There are at least two important types of such shortcomings in the URAA; firstly, deficiencies in the methodology provided for AMS calculation in terms of its applicability to existing non-exempt support measures, and secondly, deficiencies in the specification of the ‘green box’ of exempt programs with respect to its practical applicability in DCs and TCs.

The first category is not discussed at length here. The main point is that there are several such deficiencies, as the following list, which is not exhaustive, illustrates:

- 1) The unfairness of countries with non-zero ‘Total AMS’ commitments enjoying a single domestic support limit applying at the aggregate only, while countries with zero ‘Total AMS’ commitments effectively face disaggregated, product by product limits<sup>25</sup>.
- 2) Lack of provision for calculation of price support when payments in kind (barter arrangements) are involved. Suppose, for example, that farmers are paid for part of their grain with fertiliser, at the rate of 1 tonne for every 2 tonnes of grain delivered. No guidance

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<sup>25</sup> When the ‘Total AMS’ limit is at zero it automatically implies the existence of product-specific AMS commitments (for each product, at the ‘de minimis level) and a separate limit on non-product-specific AMS (at the ‘de minimis’ level). Consequently, countries in this position (mostly DCs and TCs) face a more stringent obligation than that faced by other countries (including most OECDs) which have non-zero ‘Total AMS’ limits.

is provided in the URAA as to how a calculation (equivalent to a price-gap approach) might be undertaken to determine the level of price support involved.

- 3) Lack of adequate provision for situations of high inflation. Countries were given the option of taking their 'Total AMS' commitments expressed in terms of a different currency<sup>26</sup>. Article 18.4 vaguely requires member countries to "give due consideration to the influence of excessive rates of inflation on the ability of any Member to abide by its domestic support commitments" in the review process during the implementation period. However, the need to consider carefully the timing of receipt of payments by farmers (and, therefore, of having and using exchange rate data on a monthly, if not weekly basis) was not explicitly recognised. If there is 100% inflation, and farmers do not receive payment until 6 months after delivering their crop, the calculation of the level of price support can be very different if the delay and the effect of inflation are taken into account.
- 4) Lack of provision for calculation of support implicit in the public forgiveness of farm debt. In some TCs in some years of the 1990s such appears to have been the most important element of support (in terms of fiscal cost). Forgiven loans should presumably be treated as grants. This raises the question as to whether the support should be credited to the year in which the loans were made or the year in which they were forgiven, which may beg the further question as to when farmers began to anticipate that their debt would be written off. The URAA modalities do not address these issues.
- 5) Lack of provision for how to deal with cases of negative MPS (when domestic price is maintained lower than the free trade parity price), in the calculation of AMS levels.

Even more important, in my view, is the failure of the URAA to provide practicable and internationally acceptable alternative ways for DCs and TCs to pursue their farm income augmentation and stabilisation goals. And of these, I believe the stabilisation goal is actually the more important<sup>27</sup>.

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<sup>26</sup> Among those countries which have used this provision, there is considerable inconsistency in its interpretation and application.

<sup>27</sup> Stiglitz (2000) discusses the difficulty poorer countries can have in coping with external shocks after opening up their trade, given their lack of resources and weak or non-existent safety nets. McCalla &

WTO rules in agriculture are not about constraining member countries' policy goals but about constraining, in the collective international interest, the instruments used to pursue them. DC/TC governments' needs and desires to both augment and stabilise their farmers' incomes are at least as legitimate as those of OECD governments<sup>28</sup>. Their interests in stabilising food prices are arguably more legitimate<sup>29</sup>. But, in the light of the WTO disciplines which rule out the use of quantitative import restrictions, and of 'structural adjustment programs' which aim to phase out domestic price controls and monopoly or intervention purchasing by parastatals, how are such stabilisation goals to be pursued? Theoretically, there are three possible broad policy approaches in the more market-oriented environment, - using variable direct or indirect price subsidies (e.g., 'deficiency payments'), using 'decoupled' income support payments, and using variable tariffs ('passive' market price stabilisation).

First, suppose fiscal resources are not the principal constraint. With their more generous de minimis, DCs are permitted to provide 'non-exempt' (i.e., more trade-distorting) forms of product-specific support up to 10% of the value of the product concerned, plus an equivalent amount of non-product-specific support, without penalty, in perpetuity (for TCs which don't class themselves as DC's, the corresponding figures are 5% and 5%). It is very unlikely that most such countries would want, or have the fiscal resources available, to contemplate a greater level of regular augmentation of farm incomes than this. However, provision of an insurance or safety-net against periodic sharp (i.e., of a magnitude possibly well beyond 10%) down-turns in world market prices is a different matter. Here the level of the de minimis exemption (even at

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Valdes (1999) point out that, exposed to market risk and without access to risk markets, farmers in DCs can be expected to under-invest in risk prone sectors. One of the findings of the seminal World Bank study in the early 1990s (summarised by Schiff & Valdes, 1995) was that, regardless of their other less desirable features, direct agricultural interventions by the sample of DC governments had the positive impact of, on average, reducing price variability by 32% for producers and 23% for consumers.

<sup>28</sup> It might be argued that the lack of access to commercial risk markets in those countries makes government action more imperative.

<sup>29</sup> Food expenditures typically absorb a much higher percentage of household income in such countries. Food riots prompted by price rises of staples have been experienced in many in the past, - one of the most recent examples being those prompted by rice price rises in Indonesia in 1998.

10% of the value of production) may be too low to allow the required level of non-exempt payments in some years.

What, then, about exempt ('green box') options? As already discussed, the typical structure of the farm sector in DCs and TCs, together with the lack of statistical and other infrastructure, make targeted farm income safety-net payments impractical in most of these countries. Any form of direct payment to farmers, even 'disaster payments', normally implies the need for a rural farm/household information system and a delivery mechanism far more sophisticated than what most of these countries currently possess. Furthermore, consumer food price levels remain an important political concern in many of them, and the Annex 2 criteria for targeted food subsidies are similarly inappropriate to their situation, or for widespread compensation for periodic high world market price levels.

Irrespective of WTO constraints and practicality considerations, however, fiscal affordability is likely to rule out significant use of the first two theoretical stabilisation options for many DC/TC countries.

Thus it appears that the first and second broad approaches to stabilising support measures (direct or indirect price subsidies; decoupled income support payments) are not realistic options for most DCs and TCs. First, they are fiscally much too costly. Second, they run up against WTO and/or practicality constraints. I therefore conclude that there is not a feasible way for most of these countries to achieve some acceptable degree of stability in producer incomes and consumer food expenditures in the near future other than through the use of tariffs which are applied flexibly, and given that tariffs are the only legitimate border measure to remain<sup>30</sup>.

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<sup>30</sup> Some possible other options (special safeguards, food security stocks, limits on exports) are suggested by Konandreas & Greenfield (1997), who nevertheless recognise limitations in each case to their widespread practical use by developing countries.



This third option, - varying tariffs in order to achieve an acceptable degree of domestic market price stability, - is also the only one of the three options to offer a means to consumer price stability (in addition to producer price and income stability). It has the disadvantage that, in the absence of a country having some scope to use export subsidies (the case for most DCs), it is only practicable for imported commodities.

I further conclude that such countries must be allowed to retain some scope for using variable tariffs as a stabilisation and safety net measure, in order to give a sufficient level of comfort to farmer and consumer political interests to allow them to accept the other agricultural disciplines<sup>31</sup>. But the legitimacy of this third option under the new disciplines is in some doubt and under threat.

#### 4. VARIABLE TARIFFS: FORMS; TREATMENT IN THE URUGUAY ROUND; CURRENT SITUATION

##### Forms of variable tariffs

The ways in which applied tariffs have been changed over time range all the way from occasional changes officially notified well ahead of implementation (e.g., via publication in a Government Gazette) through to unpredictable changes for every shipment, completely at the discretion of the customs officer on duty. It seems reasonable to assume that the former does, and the latter does not, conform to the principles of transparency and predictability and to the

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<sup>31</sup> The possibility of the use of variable tariffs to protect domestic markets against price fluctuations in international trade being treated as a S&D issue in the next MTN round has also been raised by Tangermann & Josling (1999, p.12), without revealing whether the idea has their endorsement. It might alternatively be argued that an implicit concession along these lines was already made in the URAA, as many DCs emerged from those negotiations with bound tariffs set well above applied tariff levels, and some have used the 'tariff room' thus created to vary applied tariff levels as a domestic price and producer income stabilising device. Under this interpretation, the current proposal may boil down simply to a call for confirmation, formalisation and clarification of the UR outcome; i.e., of providing some legal certainty to the (DC) practice of varying their applied tariff levels within their bound levels.

spirit of WTO disciplines. In between are a variety of schemes which involve infrequent, ad hoc responses to serious changes in world (import offer) price levels or systematic changes to the applied tariff in a predetermined way based on one or more reference prices or some other objective and transparent criterion. A listing of the main possibilities in the latter group follows<sup>32</sup>:

VILs, as used by the EU, were adjusted daily, according to the difference between some world market reference price and an internal target or controlled price. The lower the world price then the higher the VIL applied. If the external market price rose above the desired duty-paid entry price then the VIL would be zero. For most cereals, the entry ('threshold') price has been limited to 155% of the 'intervention' price under the terms of the URAA, and the 'new VIL' is now established fortnightly.

MIPs, as applied by the EU, have much the same effect of ensuring that the landed (duty-paid) price is not below a predetermined desired minimum. A difference is that, rather than a world market reference price, the invoice price associated with each shipment is compared to the MIP, in determining the appropriate level of duty. This difference creates a possibility for part or all of the economic rent implicit in the price gap to be captured by the exporting firm (perhaps in collusion with the importing firm) rather than by the importing government. Another difference is that, beyond the MIP level, further rises in import offer prices (world prices) do not bring further reductions in the duty payable.

Price Band systems involve changes in the applied rate of tariff only if the import offer price falls outside a predetermined range. In this case, a limited amount of transmission of world price signals to domestic producers is allowed, being only cut off when it becomes 'unreasonably' severe.

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<sup>32</sup> The interest here is in variations in applied tariffs which stay within the limits of tariff bindings, and which are non-discriminatory. Additionally, there are a range of WTO-sanctioned ways to legitimately raise the applied tariff even above its bound level, and/or in a discriminatory way, under certain special circumstances. These include anti-dumping duties, countervailing duties, ordinary safeguards, and special agricultural safeguards.

All three above variable tariff possibilities fall within the general category of sliding scale tariffs; i.e., tariffs which are inversely related, in one way or another, to the level of import prices. Additionally, seasonal changes in tariffs are sometimes used, usually for perishable products, to provide more protection for domestic producers during the harvesting and marketing season.

#### Background to the UR treatment of Variable Tariffs

VILs and, in the case of exported products, their counterparts, (variable) export restitutions, have been a fundamental component of the EU's Common Agricultural Policy (CAP) for approximately 30-40 years. They were applied to most agricultural products, and provided a means by which internal EU market prices could be kept stable in the face of fluctuating world market prices and seasonally fluctuating EU production. In short, they insulated EU producers and consumers from the world market, as discussed in section 3 above. As a significant part of overall world market supply and of demand for many products, the EU's failure to help dampen world price swings with such normal production and consumption responses was perceived to have the effect of increasing significantly the amplitude of those price swings. In effect the EU, by its actions, was refusing to share in the absorption of supply or demand shifts originating in other countries, but also forcing all the burden of absorbing the effects of its own supply shifts onto others.

Countries which were price-takers on the world market, - in particular small agricultural exporting countries, - bore the costs of this additional world price instability which the EU's policies were generating<sup>33</sup>. Little wonder that, for these countries, VILs had become an anathema by the beginning of the UR. 'Minimum import price' (MIPs) schemes, used, for example, by Japan for pork and the EU for some fresh fruits and vegetables, were perceived to

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<sup>33</sup> More rigorous underpinning for (and some qualifications on) this assertion can be found in Bale & Lutz (1979), Zwart & Meilke (1979) and Zwart & Blandford (1989).

have somewhat similar effects. The US and the Cairns Group took a strong stand against all these variable tariff measures in the ensuing negotiations.

### The UR outcome

This was the climate in which, although arguably no more than ‘variable tariffs’, VILs and MIPs were classed among the “non-tariff barriers” to be eliminated through ‘tariffication’ in the UR<sup>34</sup>. Some other already-existing forms of variable tariff mechanisms, such as those associated with ‘price band’ schemes, were not, however, explicitly classed as NTBs<sup>35</sup>. Furthermore, the mechanism with which the EU replaced its VILs, at least for cereal grains imports, arguably bears a strong resemblance to the old scheme, and its ‘entry price’ mechanism for fresh fruits and vegetables is still effectively an MIP requirement. Japan also appeared to change its MIP scheme for pork only minimally. Thus a rather confusing picture emerges about what was actually agreed in the UR with respect to the ability of countries to vary levels of applied tariffs generally. What is it that distinguishes ‘acceptable’ ways of varying applied tariff levels from ‘unacceptable’ ways, always assuming that tariff bindings are respected<sup>36</sup>?

Conceptually, this problem extends beyond agriculture. There is a general expectation that all border charges should be consolidated in a single tariff for each product, that a country’s tariff schedule be published and easily accessible to other countries’ exporters, and that public notice of tariff changes be given a reasonable time ahead of actual implementation. It could perhaps be argued that the EU’s old VILs were subject to frequent changes at short notice and did not satisfy this latter requirement, whereas Chile’s price band schemes are more transparent and do.

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<sup>34</sup> Refer URAA, Article 4, Paragraph 2 footnote 1.

<sup>35</sup> Some argue that the words “...and similar border measures other than ordinary customs duties, ...” in the same footnote (op. cit.) provide a ‘catch-all’ which extends the intended discipline to cover price band schemes (e.g., Carson, 1995), while recognising that only a formal decision through the dispute settlement mechanism would resolve this question.

<sup>36</sup> Not to be confused with the distinct but related question about when tariff bindings may be legitimately exceeded. Safeguards, anti-dumping duties and countervailing duties all represent WTO-legitimate ways in which, under certain circumstances, a country may ‘temporarily’ raise its bound tariff when trade pressures affect its domestic price level.

In summary the outcome of the URAA with respect to variable agricultural tariffs was as follows:

- 1) The EU effectively retained the use of (at least some) VILs.
- 2) The EU and Japan both effectively retained the use of MIPs.
- 3) About 8 Latin-American countries retained the use of price band schemes.
- 4) Many countries retained the use of seasonally-varied tariffs.
- 5) Many DC's, although lacking a formal program of systematically varying applied tariffs, retain considerable scope for introducing such a policy, or at least for changing their applied tariff from time to time on a more ad hoc basis, because of tariff bindings which are well above currently applied levels<sup>37</sup>.
- 6) Although the WTO-legitimacy of such deviations from "ordinary customs duties" remains untested and subject to some dispute, it would seem to be generally-accepted that schemes which operate transparently, result in predictable tariff levels, result in less frequent tariff changes, and allow at least some transmission of world price changes to the domestic market are more likely to be found in conformity.

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<sup>37</sup> For examples, of 36 sub-Saharan African member countries, 19 bound tariffs (uniformly, in most cases) at 100% or more, and 10 others bound tariffs between 50% and 99%. In South Asia, the simple average of over 600 bound agricultural tariff lines was over 100% in each case for India, Pakistan and Bangladesh. In most of these cases the corresponding applied tariffs are relatively low (FAO, pers. Comm.). Some specific African country examples of this were provided by Harrold (1995): In each case the first figure is the average % agricultural tariff binding, and the second figure is the average applied agricultural tariff: Ghana (98, 22), Kenya (100, 44), Nigeria (230, 47), Senegal (180, 44), South Africa (40, 7), Zimbabwe (161, 24).

Post-UR developments in this regard

Clearly there has been some pressure, from certain OECD countries in WTO accession negotiations, for acceding TCs (e.g. Russia) and DCs to accept tariff bindings at or close to currently applied levels. This would, among other things, minimise the possibility for them to adopt variable tariff schemes as stabilisation tools in the future. Similarly, at least one acceding country (Ecuador) was persuaded to agree to phase out its existing price band schemes, as part of the terms of accession (WTO, 1999). There appears to be less evidence of bound tariff rates which are well above currently applied rates, in the schedules of DCs and TCs which have completed accessions since 1994, than there was in the UR schedules of DCs who were founding WTO members.

There seems to be a common perception among the OECD group that allowing many DCs to ‘get away with’ high levels tariff bindings in the UR was a regrettable mistake. Certainly, DCs acceding since the UR concluded are not being accorded the same treatment, and there seems to be no inclination to extend the concession to TCs which do not want to claim DC status.

## Summary

On the one hand, many countries are using variable tariffs, in one form or another<sup>38</sup>. Under new, more euphemistic pseudonyms, variable import levies (VILs) continue to be used by the EU and minimum import prices (MIPs) by the EU and Japan. Several Latin American countries have formal ‘price band’ systems of changing applied tariffs in response to import price changes<sup>39</sup>. Many countries regularly vary some of their tariffs according to the season.

On the other hand, variable import levies, minimum import prices, and “... similar border measures other than ordinary customs duties, ...” have been explicitly banned in the URAA text

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<sup>38</sup> Of course, countries may sometimes change their applied tariffs for reasons other than stabilisation, e.g. to generate revenue.

(Article 4, Paragraph 2, footnote). There was strong pressure among OECDs in the UR to bind ordinary tariffs at close to currently applied levels, in order to make the reduction and binding commitment more meaningful. Also, there has apparently been pressure in recent WTO accession negotiations on countries which already had price band policies to phase them out, and for new members to accept tariff bindings at levels which would leave them little scope for such policies in the future.

There is thus a good case for existing WTO philosophy and disciplines in this area to be clarified, and to be interpreted and applied more consistently. I would go further, and suggest that the result of such clarification should be to explicitly allow retention, by DCs and TCs, of the right to use this third broad approach to farm income stabilisation.

## 5. PROPOSED NEW DISCIPLINE

### Design considerations

It has been recognised that some features of the URAA would cause world agricultural prices to be more stable while other features act in the opposite direction (Greenfield et al, 1996). There has hardly been enough lapsed time to allow empirical testing of this yet, but the current expectation of many is that the overall net impact of the URAA would be a very slight increase in world price stability. This means that we can expect world prices to continue to exhibit considerable instability in the foreseeable future. For example, to put this in very rough perspective, we could probably expect wheat prices to range anywhere between \$100/tonne and \$200/tonne, and not be too surprised if they occasionally move outside this range at either end<sup>40</sup>.

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<sup>39</sup> Chile, Colombia, El Salvador, Ecuador, Guatemala, Honduras, Nicaragua, Peru (IATRC, 1994)

<sup>40</sup> In fact, in the decade 1986/7 - 1996/7, annual average US Gulf port prices for wheat, corn and soybeans all moved over a range of about \$100/tonne, the percentage variation being highest for corn and lowest for soybeans (FAPRI, 1997). Wailes (this conference) showed variations in annual average California rice

Let us assume that the above illustrative numbers are ‘in the ball park’, that the expected average (‘long term trend line’) world price for wheat is \$150/tonne, that trading costs are zero (for simplicity), and that a DC wishes to use applied tariffs in a flexible way purely as a domestic price stabilising tool. Then that DC would need to have the freedom to impose a temporary tariff of 50% when the world price goes down to \$100/tonne. It may be willing to cap its protection at this level (pass on to producers the incremental effects of occasional world price drops below \$100/tonne). It may also be willing to let its producers absorb the first \$10/tonne of market decline (price band concept), in which case the ‘tariff room’ it needs may be reduced to 40%. Either way, the applied tariff would be zero when the world price was \$150/tonne, and when the latter rose to \$200/tonne, export taxes and import subsidies, - both in the order of \$50/tonne (\$40/tonne in the event of a price band of \$20/tonne, centered on the mean of \$150/tonne) , - would be needed to stop the domestic price from rising.

Such a purely stabilising use of a variable tariff (in combination with variable export taxes and import subsidies) would not cause a transfer from consumers to producers, nor significantly affect wheat production, on average over time. Over the long haul it could be fiscally neutral, with tariff revenues in some years funding import subsidy expenditures in others. It’s disadvantage, to other countries, would be it’s contribution to increased world market price instability.

The opposite extreme would be where a country wanted to use its tariff purely as a producer income-augmenting tool. In this case it would apply its 50% tariff all the time, domestic wheat price would range from \$150/tonne to \$300/tonne, large transfers from consumers to producers would be implied, production would be stimulated, consumption and imports would be depressed, and significant net fiscal revenues would be generated. Internationally, such tariff use would not be expected to make the world price more unstable, but would tend to depress it.

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export prices over the last 20 years in the \$300 - \$500 /tonne range. Recently, significant percentage declines in world market sugar prices have been reported, and over the period 1950-1990 these ranged widely



Such a ‘sock it to the consumers’ use of tariffs is typically found only among rich countries; i.e., in countries which could afford to augment their producers’ incomes in other, less trade-distorting ways. There is therefore no reasonable case for not reducing bindings on tariffs used this way.

Of course there are many conceivable tariff use options in the range between the two above extremes.

Most DCs and TCs, in addition to wanting to provide a ‘stop loss’ on declines in producer prices, will also be anxious to avoid major increases in consumer prices. For this reason they are likely to want to use tariffs mainly as a stabilising tool; i.e., be closer to the first scenario above<sup>41</sup>. This is borne out by the empirical observation that such countries are, on the whole, continuing to apply tariffs at levels well below their WTO bound rates most of the time. When world market parity prices rise above trend levels (or desirable domestic levels otherwise defined) they may choose to use export controls rather than export taxes, and to maintain food security stocks to replace imports rather than use import subsidies, but the effects will be similar. In other words, if such countries have tariff bindings for wheat of 50%, they are likely to apply a zero tariff roughly half of the time (when world prices are above trend) and vary the applied tariff between 0% and 50%, inversely with world price levels, the rest of the time; - rather than maintaining the tariff permanently at its bound rate, which could have adverse consequences for consumers. The average applied tariff over time could thus be expected to be in the 10%-15% range in this scenario. In the case of wheat, a 50% tariff ceiling binding may be sufficient to satisfy such countries. Conditions attached to the application of the tariff within the 0-50% range could conceivably also be acceptable to them. As an incentive for DCs to restrict their

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between \$250 and \$750 /tonne (constant 1990 dollars) and occasionally beyond.

<sup>41</sup> There is also often another, less well-recognised reason for such countries to exercise caution in raising domestic prices. Attempts to raise domestic prices for imported products for which the self-sufficiency level is already relatively high can often be futile. This derives from a large difference between import-parity and export-parity prices when trading costs are high (e.g., for maize in some land-locked African countries). In such situations, higher producer prices may stimulate domestic production to the point where the country changes to a marginal net export basis. In such a situation, a significant fall in domestic prices (or at least a period of quite unstable domestic prices), even when world prices are stable, becomes a real possibility.

tariff use to a predominantly stabilising function, further (future) formula reductions in tariff bindings could be related to the average ratio of applied tariff levels to bound tariff levels, observed over a prior time period<sup>42</sup>.

It has been argued here that the DC/TC need for the ability to use tariffs as a stabilisation tool derives principally from their lack of fiscal resources, which rules out other stabilisation options. The corollary of this is that such countries' need would logically last only as long as their tax revenues were limited. Complete 'graduation' from entitlement from such an S&D concession could reasonably be related, for example, to per capita GNP level; for those DC/TC countries whose tariff bindings were made subject to 'adjusted' formula reductions over time, the adjustment would cease upon 'graduation'. Some self-designated 'DC' and 'TC' countries would probably be classed as undeserving and ineligible from the outset.

#### Suggested S&D agricultural stabilisation modalities

- 1) Available to qualifying DCs/TCs only<sup>43</sup>, and for a limited number of imported and important (perhaps 'staple') products which each would nominate.
- 2) At the option of each DC/TC, and subject to certain conditions being met and incorporated in the country's schedule, a 'de minimis' level of tariff binding (at, say, 50%), beyond which further formula minimum reductions would not be required, could apply to selected imported products<sup>44</sup>.

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<sup>42</sup> As an example, suppose an across-the-board formula minimum reduction of 12% in DC bound tariffs was negotiated. Then there could be provision for the rate of reduction to be adjusted downwards to the extent there had been bound tariff 'under-fill' in a previous period. In our example, if the observed average applied rate was 12.5% and the bound rate was 50%, then the adjustment factor could be 0.25 (= 12.5/50). The required rate of reduction in the bound tariff (after adjustment) would then be 3% (=12\*0.25).

<sup>43</sup> Some richer countries which still choose to label themselves as "DCs", like Hong Kong, Singapore, Brunei, South Korea and Turkey, and conceivably also some TCs, would presumably be excluded from eligibility.

<sup>44</sup> Strictly, this would be just a 'temporary' or 'initial' universal "de minimis", as it is envisaged that it would be subject to adjustment in subsequent negotiations, probably to a different degree for different countries

3) Conditions<sup>45</sup>:

- a) Identification of a published world market reference price on which tariff adjustments would be based, and specification of frequency of adjustments to be made;
- b) Identification of a trigger level for this price, above which applied tariff levels would be zero;
- c) Specification of a formula relating the applied tariff level to the difference between the trigger level and the actual level of the world reference price;
- d) Specification of the currency used to express the prices in the formula (which implicitly indicates whether the stabilisation tool will also cover exchange rate risk);
- e) Specification of frequency of applied tariff re-calculation and potential adjustment.

Summary assessment of benefits/costs of such an S&D concession to affected LDCs/TCs

- it would offer a means to provide a price/income safety net to producers of import-competing products;
- it would facilitate acceptance of low or de minimis AMS limits and low or zero export subsidy limits; farmers' representatives who are uneasy about the apparent 'north/south' or 'east/west' (Europe) imbalance in the commitments would be able to point to something which the OECD group does not have;
- it would provide an affordable option: implementation cost would be small and it would be a significant (albeit irregular) source of fiscal revenue; - potentially providing funds for periodic domestic-price-stabilising import subsidies, or other agri-food sector initiatives;

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and products (based on their history of applied tariff use in the interim), - which would mean that it would lose its 'universal' character and become country/product-specific.

<sup>45</sup> Like other items and numbers in a country's schedule, these items and numbers could be negotiable. If to differ between countries and/or products, modality guidelines could be prepared to indicate what would be generally acceptable and how certain numbers should be derived.

- such protection from the effects of world price downturns is probably necessary for the survival of import-competing sectors in the period during which further infrastructure development and structural adjustment (at a socially acceptable rate) is taking place;
- the country could be allowed to retain flexibility of choice about whether to allow the benefits of world market price upturns to accrue to producers or whether to protect consumers (via temporary export taxes, disbursement of food security stocks, import subsidies, etc.);
- some distortion of resources towards import-competing products could occur, but distortions away from risk-prone products may be prevented<sup>46</sup>;
- provision could be made for DCs with tariff bindings already lower than the agreed (standard initial) optional de minimis binding (50% in our example) to retrogressively choose the new option (raise their bindings), provided they meet the conditions.

#### Assessment of benefits/costs to OECDs and other DCs/TCs

- it would apply only to agricultural products for which DCs/TCs are in a net import position (existing export subsidy disciplines and limits would remain firm);
- as the shares of such countries in total world imports for the products concerned (whether predominantly OECD or DC exports) is relatively small, and as much of their internal production and consumption is relatively market-price-insensitive, the marginal increase in world price instability due to the added marginal insulation of such markets can be expected to be modest;
- this S&D concession would put beneficiary countries into a much better position (in domestic political context) to accept/implement other agricultural disciplines, thus facilitating MTN or accession negotiation progress;
- modalities could be negotiated, in the form of incentives relating to future rates of adjustments to the ‘country-specific de minimis’, to ensure variable tariffs are used as a

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<sup>46</sup> Such distortions are likely to be small and offsetting, and economic efficiency arguments swamped by political ‘food self-sufficiency’ arguments, in my view.

predominantly stabilising tool, with a minimal element of income augmentation (permanent protection).

- the concession would last only as long as the DC remained eligible (e.g., below a certain GNP per capita level): once the ‘graduation’ point was reached, the S&D concession would be removed, and the bindings would become subject to unadjusted minimal formula reductions, as agreed in negotiations.

## 5. CONCLUSIONS

- 1) The URAA provided few benefits to DCs and TCs in terms of improved real access to OECD markets. Clearly this needs to be redressed in the next round, and there are already several proposals about approaches which would contribute to a correction of the imbalance. Another important way in which the special needs of DCs/TCs could be addressed is by introducing new S&D provisions in the agricultural market access area.
- 2) There is a great political need in most OECDs for governments to intervene to stabilize agricultural prices and incomes. This need is no less in DCs/TCs (arguably more in some cases).
- 3) Most DCs and TCs have very limited fiscal resources. Stabilisation options involving direct payments which are available to OECD countries are effectively unavailable to DCs/TCs. Even where fiscal resources are less limiting, traditional provision of indirect stabilisation through controlled prices offered by purchasing parastatals is being phased out for broader reasons, and targeted direct payments require a more developed information and delivery infrastructure than is available in these countries. Contrary to what some authors have claimed or inferred, the URAA does not provide realistic options for DCs/TCs broadly to pursue stabilisation goals other than through the use of variable tariffs.

- 4) By allowing DCs to take ceiling bindings at levels well above currently applied levels, the URAA opened the door to the possibility for these countries to raise and lower their applied tariffs as a domestic stabilisation tool. This should not be seen as a mistake, nor the practice portrayed as of dubious WTO-legitimacy. Rather, steps should be taken to confirm the acceptability of the practice, present the outcome as an important S&D concession, and even facilitate some upward revision of the tariff bindings of DCs who did not originally avail themselves of the opportunity. Similarly, in new accessions, the same opportunity should be extended to TCs.
  
- 5) The main URAA failure was in the high tariff bindings accepted for sensitive products in OECD countries which, once recognised as generally prohibitive to new trade, led to a last-minute scramble for other alternatives to achieve immediate improvements in access. Among other things, this, in turn, resulted in the EU being allowed to effectively retain its VILs, and both the EU and Japan to retain their MIPs, - in clear contravention of Article 4, Paragraph 2. As long as such variable tariff mechanisms are used by some OECDs, it appears very hypocritical for any OECDs to be arguing that the much more innocuous price band schemes are of doubtful WTO-legitimacy or to be trying to discourage their use by DCs. Efforts would be better spent in clarifying the aforementioned URAA Paragraph and its footnote, in determining what may remain untariffed in the longer-term, and in formally adding a dimension of S&D provisions in this area.
  
- 6) The new MTN round needs to facilitate the use by DCs/TCs of variable tariffs as a stabilisation tool. Such an S&D concession would ensure the availability of a practicable safety net option for such countries, at least for import-competing products, and thus enhance the domestic acceptability of the whole package of agricultural disciplines for them. A useful way to do this may be to borrow the concept of 'de minimis' from the domestic support area, and apply it as a level of tariff binding below which DCs/TCs would not have to reduce further, until such time as they had reached a stage of development where fiscally-funded stabilisation options were sufficiently affordable and practicable. Use of a tariff 'de

minimis' binding could be made conditional on a country agreeing to administer its applied tariff in a very predictable and transparent (or even pre-negotiated) way, and 'rate-of-future-reduction' incentives could be built in to induce DCs/TCs to use their applied tariff predominantly as a stabilisation (rather than permanent protection) tool.

In summary, it is argued that the concession proposed here would be time-limited (tariff bindings could still be gradually reduced), and would cost OECD countries relatively little in terms of greater instability of world market prices while it was in effect. It could be circumscribed to be more predictable and transparent than the old, reviled EU 'variable import levies' (VILs). And in the absence of export subsidies, its use would be confined to imported products.

Nevertheless, in my judgement, it would greatly increase the political acceptability of the URAA to farmers' organisations in DCs and TCs and hence the ability of their governments to sign on (new members) and adhere (existing members) to the current ensemble of WTO agricultural disciplines.

The real test of the validity of these arguments, of course, will be whether DCs and TCs themselves pick up on them. It is somewhat ironic that most papers about the needs and interests of DCs/TCs going into the next MTN round have been written by OECD nationals.

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## ABBREVIATIONS

AMS	Aggregate Measure of Support
DC	developing country
EU	European Union
FAO	Food and Agriculture Organisation (of the UN)
GNP	gross national product
GSP	Generalised System of (tariff) Preferences
IATRC	International Agricultural Trade Research Consortium
LDC	least developed country
MFN	'most favoured nation' (effectively "all WTO member countries") ( In the US, the synonymous term "normal trade relations" (NTR) is nowadays preferred because it avoids the connotation of preferential treatment)
MIP	minimum import price
MPS	market price support
MTN	multilateral trade negotiation
NGO	non-governmental organisation
NTB	non-tariff barrier (to trade)
OECD	Organisation for Economic Cooperation and Development (used in this paper as an abbreviation for "developed countries")
QR	quantitative restriction
S&D	'special and differential' (treatment of developing countries in the WTO)
TC	'transition' country (in process of transition from a centrally-planned to a market-based economy) (n.b. more restrictive usage in this paper to exclude some East European countries accepted, in principle, for future EU membership)
TRIMS	(WTO) Agreement on Trade-Related Investment Measures
TRIPS	(WTO) Agreement on Trade-Related Aspects of Intellectual Property Rights
TRQ	tariff-rate quota
UN	United Nations
UNCTAD	UN Conference on Trade and Development
UR	Uruguay Round (of MTNs)
US	United States of America
URAA	Uruguay Round Agreement on Agriculture
VIL	variable import levy
WTO	World Trade Organisation