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The WTO negotiation on agriculture and the common agricultural policy

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The WTO Negotiation on Agriculture and the Common Agricultural Policy²

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1 Introduction

This note briefly discusses the linkages between current WTO negotiations on agriculture and the on-going CAP reform process. Before discussing the implications for the CAP of the possible outcome of current negotiations, an assessment of the impact of the implementation of the 1994 GATT “Agreement on Agriculture” (AoA) for the agriculture and food sector in the EU and for the CAP is offered. Then, the linkages between the CAP reform process and the current negotiations are discussed. Finally, the issues currently on the agenda of the WTO negotiations are identified and the main elements of a possible final agreement briefly discussed.

2 The 1994 GATT “Agreement on agriculture” and the CAP

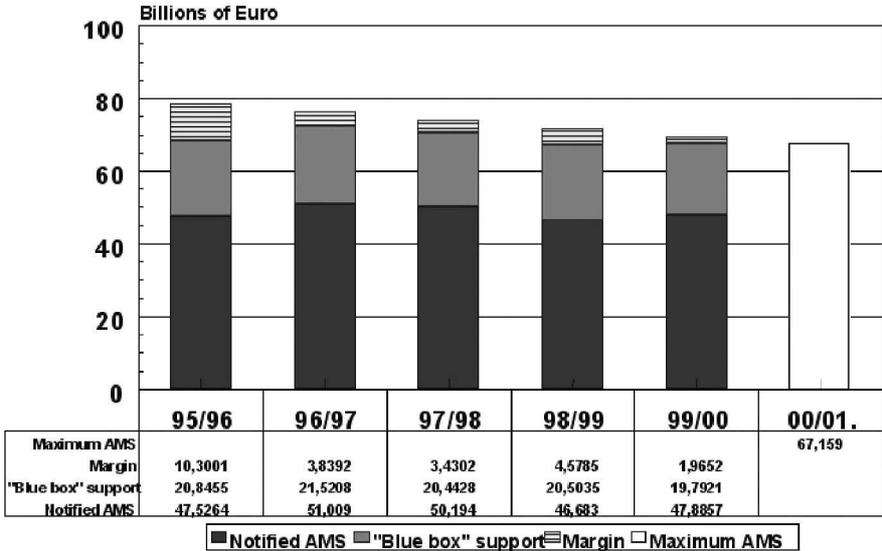
The “*domestic support*” commitment has not been a problem, neither for the EU nor for (hardly) any other country. This constraint not being binding for the EU is the result of the “blue box”, and of the fact that price support in the EU significantly declined between the “base period” (1986-88) and 1995 (i.e. the decrease in the difference between domestic and world prices). However, even if the “blue box” did not exist, in the first five years of the implementation period (those for which EU notifications to the WTO are available) support in the EU as measured by the AMS would have stayed within the limits dictated by the Agreement (Figure 1). The same should be true for year 2000 and beyond. Agenda 2000 determined a further shift of support from the “amber box” to the “blue box”; in 2002 (when Agenda 2000 decisions for the cereals and beef

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sectors are fully implemented) this shift should determine a 20% reduction (9 billion €) of the Aggregate Measurement of Support (AMS) of the EU and in an increase of the support in the “blue box” by a smaller amount.

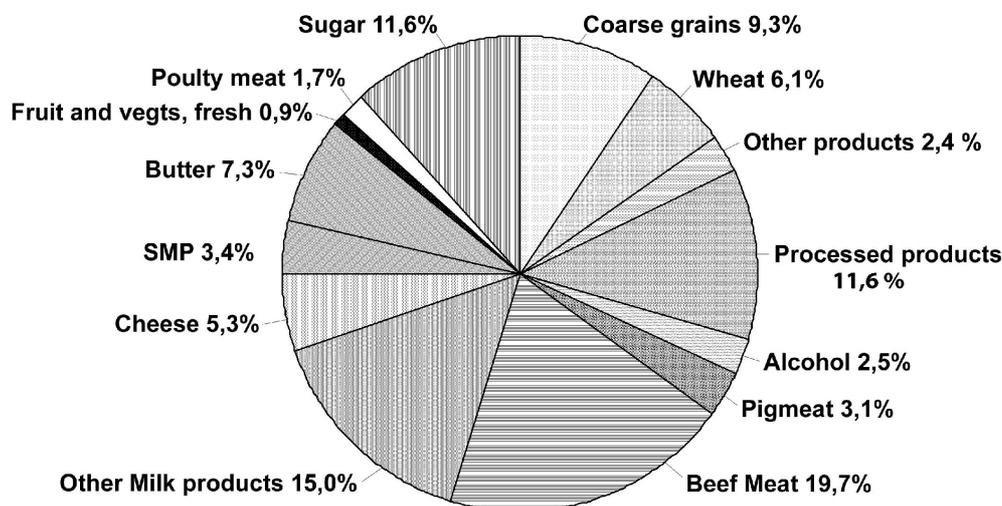
Fig. 1: European Union. Domestic support reduction commitments: notified AMS, support falling in the “blue box” and margin left with respect to the maximum allowed AMS.



“Market access” commitments did not imply a significant reduction of EU border protection, except for Tariff Reduced Quotas (TRQs) in specific markets. “Tariffication” of EU variable levies did not lower market protection mainly because of the high level of the levies in the “base period” vis a vis those in 1995. As a result of the Blair House agreement, the EU essentially kept using variable levies for cereals and rice, although giving up the option to impose higher tariffs (allowed by its high binding tariffs). For fresh fruit and vegetables, the new “entry price” system does not look different enough from the old “reference price” system to induce a significant change either in the level of protection, or in its “quality”. Tariff reductions over the implementation period were not a problem because of both the “dirt” in the tariffs resulting from the “tariffication” of variable levies, and the reduction of the distance between domestic and world prices for many commodities which occurred between the “base period” and 1995. However, TRQs were indeed a problem for dairy products and had a non marginal impact in all meat markets.

“Export competition” commitments proved to be those most often binding for the EU. The AoA had a limiting effect on EU subsidised exports in at least one of the six years of the implementation period for rice, cheese, “other milk products” (these account for almost 50% of total EU export subsidies in dairy products; Figure 2), poultry, beef, olive oil, wine, fresh fruit and vegetables (Tables 1 and 2). In several cases, including poultry meats, wine and fresh fruit and vegetables, increased non subsidised exports took place when the constraint on the volume of subsidised exports became binding.

Fig. 2: European Union - Export subsidy expenditure by product (1995-2000)



Tab. 1: European Union - Actual subsidized exports as a percentage of the maximum subsidized exports allowed under the GATT "Agreement on agriculture" (1995-2000)

| | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 1995-2000 |
|---|------|-------|-------|-------|-------|------|-----------|
| Wheat and wheat flour | 13,6 | 75,0 | 72,4 | 83,3 | 99,8 | 70,7 | 67,0 |
| Coarse grains | 48,2 | 90,3 | 69,9 | 123,3 | 161,0 | 65,3 | 91,6 |
| Rice | 54,4 | 144,2 | 50,2 | 99,0 | 100,8 | 99,2 | 99,7 |
| Rapeseed | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 |
| Olive oil | 96,4 | 103,7 | 72,6 | 0,0 | 0,0 | 0,0 | 48,3 |
| Sugar | 55,0 | 80,1 | 117,8 | 111,5 | 73,0 | 69,3 | 84,3 |
| Butter and butter oil | 30,0 | 58,7 | 37,4 | 38,0 | 46,5 | 49,4 | 43,1 |
| Skim milk powder | 72,0 | 83,6 | 56,6 | 74,5 | 146,4 | 47,0 | 79,7 |
| Cheese | 99,0 | 99,1 | 84,3 | 62,3 | 89,2 | 94,8 | 88,5 |
| Other milk products | 97,6 | 100,0 | 102,0 | 90,7 | 110,0 | 91,1 | 98,6 |
| Beef meat | 89,6 | 109,6 | 93,7 | 76,1 | 86,6 | 57,8 | 86,9 |
| Pigmeat | 69,8 | 54,8 | 42,3 | 153,8 | 149,8 | 29,0 | 82,6 |
| Poultry meat | 96,2 | 99,2 | 105,0 | 99,4 | 100,8 | 91,1 | 98,8 |
| Eggs | 75,4 | 56,3 | 90,1 | 104,1 | 96,5 | 84,8 | 83,8 |
| Wine | 75,8 | 110,7 | 114,6 | 97,9 | 98,9 | 98,9 | 99,2 |
| Fruit and vegetables (fresh) | 98,8 | 98,6 | 98,1 | 93,0 | 110,9 | 98,0 | 99,5 |
| Fruit and vegetables (processed) | 53,5 | 80,7 | 60,7 | 55,8 | 72,4 | 53,1 | 62,8 |
| Raw tobacco | 5,9 | 1,1 | 0,0 | 0,0 | 0,0 | 0,0 | 1,5 |
| Alcohol | 32,1 | 79,2 | 74,0 | 88,2 | 166,8 | 77,7 | 84,6 |

Source: EU notifications to WTO

Tab. 2: European Union. - End of the year subsidised exports “credit” as a percentage of the Uruguay round subsidised exports reduction commitments up to that year. (1995-1999)

| | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|-------|-------|-------|-------|-------|
| Wheat and wheat flour | 86,4 | 56,6 | 47,6 | 40,6 | 33,6 |
| Coarse grains | 51,8 | 31,2 | 30,9 | 18,2 | 3,8 |
| Rice | 45,6 | 1,6 | 0,2 | 0,4 | 0,2 |
| Rapeseed | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 |
| Olive oil | 3,6 | 0,0 | 8,8 | 30,3 | 43,1 |
| Sugar | 45,0 | 32,7 | 16,5 | 9,9 | 13,0 |
| Butter and butter oil | 70,0 | 55,9 | 58,1 | 59,0 | 58,0 |
| Skim milk powder | 28,0 | 22,3 | 29,1 | 28,2 | 14,5 |
| Cheese | 1,0 | 0,9 | 5,6 | 13,0 | 12,6 |
| Other milk products | 2,4 | 1,2 | 0,2 | 2,3 | 0,1 |
| Beef meat | 10,4 | 0,7 | 2,4 | 7,3 | 8,4 |
| Pigmeat | 30,2 | 37,6 | 44,0 | 21,0 | 7,9 |
| Poultry meat | 3,8 | 2,3 | 0,1 | 0,2 | 0,0 |
| Eggs | 24,6 | 33,9 | 26,3 | 19,2 | 16,4 |
| Wine | 24,2 | 7,1 | 0,2 | 0,6 | 0,7 |
| Fruit and vegetables (fresh) | 1,2 | 1,3 | 1,5 | 2,8 | 0,3 |
| Fruit and vegetables (processed) | 46,5 | 33,2 | 35,2 | 37,3 | 35,5 |
| Raw tobacco | 94,1 | 96,4 | 97,5 | 98,0 | 98,3 |
| Alcohol | 67,9 | 44,8 | 38,8 | 32,4 | 14,1 |

Source: EU notifications to WTO

When the GATT AoA was reached, in December 1993, the stand of the Commission (as well as of many others) was that the Agreement was fully “compatible” with the CAP, i.e. it did not entail introducing any binding constraint. However, as some had predicted, the Agreement did in fact introduce binding constraints for the CAP in several sectors. Subsidised export commitments will likely be binding beyond 2000/01 (when “credits” cannot be used any more and subsidised exports must remain within the commitments spelled out in the “schedules” for the last year of the implementation period) for rice, dairy products, wine and fresh fruit and vegetables.³ If Agenda 2000 had not taken place, the EU, starting in 2001, would very likely have had to face binding constraints on its subsidised exports of wheat, coarse grains, beef and poultry as well. Large increases in EU intervention stocks as a result of the AoA took place for coarse grains (in 1998 and 1999) and dairy products (from 1996 to 2000 and, again, in 2002). In general, the commitment on export subsidy expenditure has not been a problem (due to the market reorientation of most EU domestic prices), apart from rice, wine, alcohol, and “other processed products” and, to a lesser extent, sugar (leading to the reduction of quotas “A” + “B”) (Tables 3 and 4).

³ Export subsidies for olive oil have not been used since 1998 without any explicit policy change.

Tab. 3: European Union. - Actual export subsidy expenditure as a percentage of the maximum export subsidy expenditure allowed under the GATT "Agreement on agriculture" (1995-2000)

| | 1995 | 1996 | 1997 | 1998 | 1999 | 2000 | 1995-2000 |
|---|-------------|-------------|-------------|-------------|-------------|-------------|-------------|
| Wheat and wheat flour | 5,1 | 15,1 | 9,3 | 29,5 | 34,1 | 8,4 | 16,0 |
| Coarse grains | 18,9 | 26,0 | 19,8 | 60,1 | 63,0 | 18,3 | 33,3 |
| Rice | 55,5 | 141,3 | 68,6 | 58,3 | 65,3 | 87,8 | 80,0 |
| Rapeseed | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 0,0 | 27,1 |
| Olive oil | 77,8 | 52,2 | 11,2 | 0,0 | 0,0 | 0,0 | 0,0 |
| Sugar | 51,7 | 76,5 | 121,8 | 134,1 | 86,1 | 74,7 | 89,8 |
| Butter and butter oil | 18,4 | 42,3 | 25,6 | 25,4 | 32,2 | 35,7 | 29,6 |
| Skim milk powder | 34,7 | 44,8 | 32,9 | 58,4 | 111,9 | 9,5 | 48,0 |
| Cheese | 73,7 | 49,9 | 35,7 | 33,7 | 60,1 | 69,7 | 53,7 |
| Other milk products | 71,0 | 76,3 | 84,6 | 91,6 | 118,6 | 58,8 | 83,0 |
| Beef meat | 78,4 | 85,4 | 50,8 | 42,3 | 52,3 | 30,6 | 59,0 |
| Pigmeat | 34,8 | 26,4 | 29,8 | 154,6 | 115,3 | 17,7 | 61,0 |
| Poultry meat | 85,0 | 57,4 | 64,5 | 82,4 | 75,3 | 62,6 | 71,5 |
| Eggs | 21,3 | 12,0 | 24,1 | 34,3 | 29,9 | 18,5 | 23,1 |
| Wine | 88,9 | 110,6 | 74,1 | 63,0 | 61,2 | 60,5 | 78,3 |
| Fruit and vegetables (fresh) | 90,7 | 85,1 | 38,4 | 50,4 | 64,4 | 51,1 | 64,9 |
| Fruit and vegetables (processed) | 92,6 | 89,5 | 53,3 | 45,5 | 60,4 | 47,0 | 66,7 |
| Raw tobacco | 18,8 | 4,0 | 0,0 | 0,0 | 0,0 | 0,0 | 5,3 |
| Alcohol | 36,3 | 89,6 | 85,6 | 106,1 | 208,0 | 99,5 | 99,8 |
| Other processed products | 68,5 | 86,2 | 92,7 | 107 | 151,3 | 99,8 | 97,6 |
| Total | 41,6 | 51,1 | 43,5 | 58,2 | 67,6 | 37,1 | 49,5 |

Source: EU notifications to WTO.

The costs deriving from compliance with the GATT commitments in the sectors where these were binding have been borne by less competitive farmers, those selling their products at lower prices, and by taxpayers (when increased downward pressure on prices on the domestic markets deriving from the reduction in subsidised exports and TRQs led to a rise in intervention stocks). The distribution of costs between farmers and taxpayers has not been uniform among different sectors. While intervention prices for dairy products remained relatively high and profitable, intervention mechanisms for wine, fresh fruit and vegetables lost strength over time as a result of lower institutional prices and significantly reduced volumes eligible for the intervention. This meant that increased downward pressure on domestic prices as a result of the binding GATT commitments in some sectors did not find a lower limit in the intervention prices, while this was the case in others. This implied an uneven distribution across sectors of the costs of complying with binding GATT commitments among taxpayers and farmers.

Tab. 4: European Union. - End of the year export subsidy expenditure “credit” as a percentage of the Uruguay round export subsidy expenditure reduction commitments up to that year. (1995-1999)

| | 1995 | 1996 | 1997 | 1998 | 1999 |
|---|-------|-------|-------|-------|-------|
| Wheat and wheat flour | 94,9 | 90,1 | 90,3 | 86,1 | 82,9 |
| Coarse grains | 81,1 | 77,7 | 78,5 | 69,9 | 64,4 |
| Rice | 44,5 | 3,0 | 11,8 | 18,5 | 21,2 |
| Rapeseed | 100,0 | 100,0 | 100,0 | 100,0 | 100,0 |
| Olive oil | 22,2 | 34,6 | 51,4 | 62,3 | 68,7 |
| Sugar | 48,3 | 36,3 | 18,3 | 6,6 | 7,8 |
| Butter and butter oil | 81,6 | 70,0 | 71,4 | 72,1 | 71,4 |
| Skim milk powder | 65,3 | 60,4 | 62,5 | 57,8 | 45,9 |
| Cheese | 26,3 | 37,7 | 45,7 | 50,1 | 48,5 |
| Other milk products | 29,0 | 26,4 | 23,0 | 19,7 | 13,2 |
| Beef meat | 21,6 | 18,3 | 27,8 | 34,4 | 36,6 |
| Pigmeat | 65,2 | 69,3 | 69,6 | 42,0 | 32,3 |
| Poultry meat | 15,0 | 28,3 | 30,5 | 27,7 | 27,2 |
| Eggs | 78,7 | 83,2 | 80,9 | 77,5 | 76,2 |
| Wine | 11,1 | 0,6 | 8,5 | 14,8 | 18,9 |
| Fruit and vegetables (fresh) | 9,3 | 12,0 | 27,4 | 32,4 | 32,9 |
| Fruit and vegetables (processed) | 7,4 | 8,9 | 20,7 | 28,3 | 30,2 |
| Raw tobacco | 81,2 | 88,1 | 91,6 | 93,2 | 94,2 |
| Alcohol | 63,7 | 37,9 | 30,6 | 22,4 | 0,1 |
| Other processed products | 31,5 | 23,1 | 18,3 | 12,9 | 2,6 |

Source: EU notifications to WTO.

The EU is not only the first world importer of food products, but the second largest exporter. The benefits deriving to EU agriculture from other countries implementing the agreement should not be underestimated. These gains mainly derive from the more “serene” trade environment (rather than from trade liberalisation, which was very limited) as a result of the 1994 agreement, which meant lower risks and, as a result, lower transaction costs. These benefits have been harvested by the more competitive exporting segments of the agri-food sector in the EU.

3 The WTO negotiation on agriculture: where are we today?

Negotiations on agriculture started in March 2000 as a result of Article 20 of the 1994 AoA. Failure (not because of agriculture) to agree in December 1999 in the WTO Ministerial Conference in Seattle on launching a “full round”, involving many negotiating tables, resulted in the negotiation on agriculture focusing before the November 2001 Ministerial conference in Doha on a “minimalist” agenda. This was mainly due to (a) the letter of the text of Article 20, (b) a widely shared concern to try to avoid creating additional problems to the credibility of WTO through a confrontation in

the negotiation on agriculture, and (c) the limited possible trade offs in the negotiation due to the fact that each country was forced to assess benefits and costs of the agreements reached based only on concessions and gains in the only two negotiation tables (“agriculture” and “services”) that were operating.

During the first year of the negotiations countries tabled their (starting) proposals. Although these contributions need not to be evaluated *per se*, but as part of the negotiation process, in general they were less ideologically extreme and less openly confrontational compared to those produced in the first steps of the Uruguay round. This was mainly due (a) to better market conditions (more profitable prices and a much more serene trade climate) than in the late 80s; (b) to the existence of a path (that designed by the 1994 AoA) which could be used as an initial reference framework for the definition of the steps to be agreed upon in the negotiation, and, (c) again, to the shared concern to avoid a heated and loud confrontation in the delicate stage for multilateral trade negotiations resulting from the failure to reach an agreement in the Ministerial Conference in Seattle.

In March 2001 countries agreed to devote the first part of “Phase 2” of the negotiations (which ended in March 2002) to the discussion of a list of specific issues: tariff rate quota administration; tariffs; amber box; export subsidies; export credits; state trading enterprises; export restrictions; food security; food safety; rural development. The list included (explicitly or potentially) all the elements of the AoA, plus some (but not all) of the issues which have been raised by some of the main actors in recent years: export credits, state trading enterprises, export restrictions, and “multifunctionality” (the latter hiding behind the less disturbing label of “rural development”).

The Ministerial Conference in Doha, Qatar, on November 9-13, 2001 led to the launch of a new round, sending the much needed message that the *impasse* resulting from the failure to reach an agreement in Seattle had been overcome. However, the cost paid for agreeing on a new round (or for not taking any chance of a new round not being agreed upon) is the limited agenda of the new negotiations, which does not include any of the potentially most controversial issues.

With respect to the on-going negotiations on agriculture at the time, the agreement reached in Doha did not introduce any significant change, but rather confirmed the validity of the preliminary work carried out in the negotiations started in March 2000, including working toward an agreement whose framework replicates that of the 1994 AoA. With respect to other relevant and potentially highly controversial issues, such as national standards to protect human, animal or plant life and health, or labour and environmental standards, the Declaration did not really go much beyond reaffirming what little had been agreed at the end of the Uruguay round.

With the beginning of Phase III of the negotiation in March 2002 the preparatory work devoted to the tabling and discussion of initial positions and statements ended and the real negotiations which will eventually lead to the text of the agreement started. The timetable which has been agreed upon is to have an “overview paper” on the status of the negotiations prepared by the Chair of the Committee on Agriculture by mid December 2002 and a draft of the “modalities”, the technical document describing in detail the content of the agreement, ready by January 2003. This should lead to a final text of the “modalities” approved by the Committee by the end of March 2003, and the country “schedules”, the legal documents describing the actual commitments deriving to each country from the “modalities”, approved by the 5th Ministerial Conference in September. Whether this tight schedule can be honoured is something which remains to be seen. Many believe that the new US Farm Bill has made it even less likely that an

agreement can be reached in such a short period of time; this is because there is a need to internalise the shock to the negotiation produced by the severe turn in the agricultural policies in the US, a shock which cannot be absorbed in few months. Let us now briefly review what the negotiation has been focusing on.

Domestic support

Negotiations are focusing on (a) the elimination of the “blue box”, (b) a redefinition of the “green box”, and (c) how and by how much to reduce support in the “amber box”. Many countries call for the elimination of the “blue box”. While some countries call for a smaller “green box” (i.e. for more stringent rules defining policies exempt from support reduction commitments), other countries (including the EU) call for a larger one, to accommodate policy instruments aimed at achieving relevant “non trade concerns”, including food security, animal welfare and concerns related to the “multifunctionality” of agriculture. Proposals have been made to define the commitments based on a Measurement of Support calculated on a product by product basis, rather than on an aggregate basis as in the 1994 AoA, and to define reduction commitments using current AMS as a reference, rather than that in the “base period” of the AoA.

Market access

Negotiations are focusing on (a) how to reduce tariffs; what to do with (b) Tariff Reduced Quotas (TRQs), and (c) the Special Safeguard Clause (SSC); (d) limiting implicit market protection by State Trading Enterprises (STEs). Proposals on how to reduce tariffs include those to further reduce legally binding tariffs; reduce currently applied (rather than binding) tariffs; introduce a maximum tariff level (to eliminate tariff picks); eliminate all trade distortions (including export subsidies) in specific markets (the *zero-for-zero* option); reduce tariffs using a formula which induces a reduction in tariff dispersion (i.e. a formula which reduces higher tariffs by larger percentages); reduce tariffs using a formula which causes a reduction in tariff escalation (i.e. a reduction in the widespread tendency to impose on processed products higher tariffs than those imposed on raw products, in order to protect the domestic processing industry). Negotiations on TRQs will focus on their administration (when the TRQ is binding there are rents associated to imports within the quota, and allocation mechanisms become sensitive; many TRQs are not filled and, in some cases, exporters claim this is a result, not of adverse economic conditions, but, rather, of how the quotas are administered) and an increase in their volume. The AoA includes a SSC for products which have been subject to “tariffication” which allows for increased protection when imports expand above certain thresholds, or prices drop below certain levels. Exporting countries feel that the SSC limits their ability to profit from the increased competitiveness of their exports and should be eliminated, or its use drastically limited.

Export competition

EU actual export subsidy expenditure accounts for 4/5 of the total (across all countries); EU export subsidy expenditure allowed by the AoA equals 75% of the total. Negotiations are focusing on (a) the reduction or elimination of export subsidies and on limiting implicit export subsidisation by the means of (b) subsidised export credit, (c) the activities of exporting STEs and (d) “unfair” food aid practices.

Special and Differential Treatment

Negotiations will focus (a) on additional provisions specifically addressing the needs of developing and least developed countries, including special concessions and less

demanding commitments, and (b) on improving the 1994 “Decision on Possible Negative Effects of the Reform Programme on Least Developed and Net Food Importing Developing Countries”.

Other issues

Despite the “minimalist” character of the agenda of the agricultural negotiations, it does contain a few issues which cannot be seen as part of a “refinement” of the framework designed with the AoA. These include policies limiting exports, and those allowing food quality markets to develop. Some food importing countries would like export limiting policies (which make prices on the world market increase) to be made illegal, or their use strictly regulated. The EU is proposing to multilaterally recognise and enforce regulations limiting the use of certain geographical denominations identifying high quality foods whose production is closely connected with a specific location. The Doha Ministerial Declaration calls for a negotiation within the Council for Trade-Related Aspects of Intellectual Property Rights (TRIPS) “for the establishment of a system of notification and registration of geographical indications for wines and spirits” by the end of 2003 and opens the door for the extension of the results of this negotiation to other agriculture and food products besides wines and spirits.

What’s left out

Among the issues which were raised before the WTO Ministerial Conference in Seattle as items to be on the agenda of the new negotiations on agriculture which are not going to be seriously considered in the negotiations, in the sense that there is a shared consensus that the negotiation will not lead to the introduction of effective disciplines, the most important probably are (a) food safety and (b) the use of trade policies to counteract distortions in competitiveness induced by differences in national regulations concerning labour and environmental standards.

4 What’s at stake for the CAP?

If we look at the CAP as we know it today (i.e. including the full implementation of Agenda 2000, but without considering neither changes which will derive from the Mid Term Review of Agenda 2000 or those which might be needed in order for the enlargement to the Central and Eastern European Countries to take place), the elements of the WTO negotiations which are most sensitive for the CAP can be summarised as follows:

Domestic support

A further reduction of the maximum AMS *as defined in the 1994 AoA* is not expected to create any need to modify the CAP. The AMS for the EU in 1999/00 was just below 70% of the maximum allowed by the GATT agreement in 2000/01 and beyond; in addition, the full implementation of Agenda 2000 determined an additional shift of support from the “amber” to the “blue box”.

The pressure on the CAP in the domestic support area of the negotiations comes from two fronts. The first is the need to keep EU current and future “partially decoupled” direct payments⁴ to farmers exempt from the reduction commitments; the second is keeping reduction commitments linked to an AMS, rather than to a measurement of support calculated on a product by product basis. If direct payments have to be included

⁴ With the possible exception of current slaughter premiums for beef, which appear hard to defend as not being highly “coupled”.

in an *enlarged-as-much-as-needed* “green box”, they need to be modified to become (a) less trade distorting (more “decoupled”) and/or (b) linked to goals different from supporting agricultural production (such as environmental protection or animal welfare).

In this respect, the decision to fully “decouple”, although for a limited period of time, most direct payments to farms receiving less than € 1,250 per year is promising and potentially far reaching.

A shift to a product by product measurement of the support to be subject to reduction commitments would induce the need to modify the CAP in those sectors where very little change has been introduced in the recent past (dairy products would be a typical case in point). The actual relevance of such a move for the CAP would depend on the choices made on how to measure support, and on the reference “base period” to be considered to calculate the reductions.

WTO negotiations on reducing domestic support is providing additional pressure and setting a time horizon⁵ for the EU to modify the instrumentation of the CAP, and, more specifically, all direct payments to farmers. How these will be changed will be determined by a decision making process which will be mainly driven by domestic concerns and will result from the resolution of conflicts involving opposing domestic interests. In this respect WTO negotiations on domestic support commitments will play mainly the role of an external force indicated as (but not really being...) one of the main reasons for the change.

In the recent past EU domestic wheat prices have been very close to those prevailing on international markets. This makes compulsory set aside hard to justify. However, it is worth noting that if compulsory set aside were set equal to zero, current direct payments for COP crops would become no more eligible for inclusion in the “blue box” (they would lose the “production limiting” feature which makes them exempt from GATT domestic support reduction commitments).

Market access

The likely reduction of binding tariffs which will result from the new agreement is not expected to determine a significant reduction in protection for EU domestic markets. This is due to the market reorientation of many domestic prices (including grains, meats, fresh fruit and vegetables, table wine) resulting from the domestic policy reform process in the EU, with additional help from a weak Euro.

If expanded TRQs are part of the new Agreement they will potentially constitute a serious concern for the EU in those markets where domestic prices are still significantly higher than those prevailing on the world market (dairy products are, once more, the typical example).

If concerns have to be raised with respect to EU market protection, attention should be given not so much to the agreement at the end of the WTO negotiations, but to (a) EU enlargement and (b) current and future preferential trade agreements. These will likely prove to be much more relevant in providing increased access to EU markets than the tariff reduction and increased TRQs deriving from the WTO agreement.

⁵ The “peace clause” (Article 13 of the AoA) expires on December 31 2003, when all agricultural policies which are legitimate under the AoA but do not conform to general WTO rules will be no longer exempt from countervailing and retaliatory actions. The Doha Ministerial Declaration calls for the negotiations on agriculture to be completed by March 2003, with all countries producing their draft “schedules”, based on the agreement reached, “no later than the date of the Fifth Session Ministerial Conference”, which will take place in Cancun, Mexico, in September 2003.

Export competition

Further reduction in subsidised exports and export subsidy expenditure would likely create minor problems in the sectors where the full implementation of Agenda 2000, coupled with the weak Euro, has driven EU domestic prices close to those prevailing on world markets (this has been the case of wheat, for example). If we forget for a moment the market impact of the BSE crisis, lower institutional prices and lower feed grain prices were expected to considerably reduce the distance between domestic and international prices for all meats. On the contrary, further reductions in subsidised exports will induce significant problems (a) in those sectors where domestic prices are still much higher than international ones (such as dairy products and sugar), and (b) in all other sectors, in marginal farms (and areas) unable to compete at world market prices.

5 The US Farm Security and Rural Investment (FSRI) Act, the Agenda 2000 Mid Term Review and the WTO negotiations

The approval of the FSRI Act has impacted the WTO negotiations in many ways. First, the dramatic increase, with respect to the FAIR Act, of direct payments to farmers made the position of the US in the negotiation on domestic support reduction commitments much more conservative, more preoccupied to defend increased domestic support at home than to try to make other countries reduce the domestic support they provide their farmers. Second, expectations for limited liberalisation of domestic support policies, which are highly concentrated in a small number of developed countries, strongly reduces the willingness of other countries to consider accepting to liberalise their policies in other areas, such as export subsidisation and market access, strongly reducing the (already limited) expected potential liberalising effect of the final agreement as a whole. Third, the policy choice in the US provided very much needed new ammunition to those opposing for their own interests domestic policy reforms in other developed countries, which have now good ground to oppose a reduction in domestic support (*why should we do it, when “even the US” is moving in the opposite direction? Why do you want to reduce our competitiveness with respect to the US farmers?*)

The re-introduction of generous deficiency payments linked to reference prices, expected in most years to be higher than market prices, and the update in acreage and yields, makes for the US a significant additional reduction of the AMS and the redefinition of policies exempt from reduction commitments a very sensitive component of the negotiation. Most countries aligned on the vast and differentiated front of those committed to go after a significant liberalisation of domestic policies are pointing out to the “cynical hypocrisy” of the US stand and are not going to easily (and quickly) give up on their quest for a far reaching agreement.

Hence, the impact of the FSRI Act on the WTO negotiation is much stronger than that linked to its direct effect on the US stand in the negotiation itself.

In July 2002 the EU Commission tabled its proposal for the Agenda 2000 Mid Term Review. The proposal goes well beyond the minor adjustments one would expect from a mid term assessment of the policy changes introduced in 1999 with Agenda 2000; it is, in fact, a proposal for a radical redesign of the policy instrumentation of the CAP. However, the history of the CAP tells us that the proposals by the Commission are never accepted by the Council of Ministers; we can reasonably expect the final outcome of the tense negotiation which has just started will likely be much more conservative than the proposal by the Commission.

Nevertheless, it is certainly worth assessing the proposal from the point of view of the WTO negotiations. The main features of the proposal are: a 5.9% reduction of the intervention prices for cereals; a 50% reduction of the intervention price for rice; a further decoupling of all direct payments for the beef sector; and a reduction of all payments to farmers by 3% per year for 6-7 years, with the resources freed being used for what the Commission and the farmers refer to as “rural development” policies. In addition to (and, not surprisingly, separately from) these policy adjustments, the Commission proposed the replacement of all direct payments to farmers with one single farm “income support” payment, based on historical payments to the farm, irrespective of what is grown, but made conditional to the farm complying with environmental, food safety, and animal health and welfare standards. This means the decoupling of all forms of support provided to farmers by the CAP as we know it today.

Let us consider the proposal for the policy adjustments first, separately from that to decouple all direct payments. The lower intervention prices for cereals and rice and the decoupling of the payments for the beef sector only would (a) reduce the EU AMS and (b) help the realignment of EU domestic prices to world prices, reducing the pressure for intensification of production and contributing to compensate the negative effect of a stronger Euro on the international competitiveness of EU agricultural products; in turn, this would reduce the need for both, export subsidies and market protection.

In addition, if the Council opts for rejecting the Commission’s proposal for a full decoupling of all direct payments to farmers but retains the cross-compliance to environmental standards as a condition to receive direct payments as we know them today, these will become much more easy to defend as eligible for exemption from domestic support reduction commitments in a negotiation on the elimination of the blue box and on the contemporaneous partial redesign of the green one.

The EU is genuinely moving toward incorporating environmental protection goals in the CAP. Largely as a result of domestic concerns, the EU seems ready to introduce or strengthen cross compliance requirements related to farming practices as a condition to obtain direct payments. What appears to be less clear is whether farmers recognise this as a genuine strategic choice, or whether they see it just as a way to make them keep the support they have been granted in the past, “circumventing” domestic pressure to significantly reduce both such support and its undesirable effects on the environment (both seen as no longer socially acceptable). In other words, there might be a serious communication problem between European society at large and farmers, with the latter looking at environmental cross compliance constraints and at payments to induce action on their part to protect the environment as a way to keep a high level of support without really having to change the way they farm.

Of course, if the Council of Ministers agreed on accepting the Commission’s proposal for a full decoupling of all forms of CAP direct payments, these payments would be easily defensible as having minimal trade distorting effects and as being motivated by (genuine) non trade concerns, such as environmental protection, food safety and animal welfare and health domestic concerns.

In any case, the chances of the most liberalising components of the package proposed by the Commission being accepted by the Council are strongly reduced by the characteristics of the agricultural policy package approved on the other side of the Atlantic.

6 The WTO negotiations on agriculture: what may the outcome look like?

Trying to anticipate what the final agreement of current WTO negotiations on agriculture may look like is clearly a difficult and risky exercise. The new round being characterised by a relatively “minimalist” agenda considerably reduces the possibility of a far reaching agreement. Many factors will influence the negotiations and its conclusion, the most obvious ones being the policy changes which have taken place and those which are expected to take place in the near future in some of the main players; China now being a member of WTO (which is expected to lend political weight to at least some of the issues of specific interest for developing countries); unexpected market developments; and the prevailing climate in international relations (one of the factors leading to the conclusion of the Uruguay round in 1993 was the on-going joint multilateral military effort in operation “Desert Storm”).

There are three main conclusions to be drawn from how the negotiations proceeded and eventually ended in the Uruguay round which can be useful in trying to forecast what may happen in the current negotiations. *First*, the distance between the starting negotiation positions and the content of the agreement eventually reached may be quite large. *Second*, despite the multilateral nature of WTO negotiations, many elements of the eventual agreement were in the Uruguay Round largely the result of bilateral deals struck between the US and the EU. *Third*, contrary to what many believe, the EU agreed on the conclusion of the round only when the agreement was shaped in such a way to be considered fully acceptable from the point of view of its implications for the CAP. In other words, the MACSHARRY reform was “written in Bruxelles”, nor in Geneva or Washington, and it was the AoA which had to be shaped, as needed, to conform to what the EU felt acceptable.

With this in mind, the main elements of the agreement at the end of the negotiations might look as follows:

Domestic support

The “blue box” will be eliminated, but the “green box” will be enlarged as much as needed to include EU direct payments to farmers in use at the time the agreement is reached (i.e. they may be somewhat different from those we know today, for example significantly more “decoupled”, and/or associated to stricter environmental cross compliance conditions). Reduction commitments will again be defined on the basis of an Aggregate Measurement of Support (not on a product by product basis). The extent by which domestic support will be further reduced is clearly severely limited by the provisions of the FSRI Act.

Market access

Tariffs will be subject to a significant reduction (having as a reference the binding levels, not currently applied tariffs), which will lower the degree of market protection with respect to that existing in the reference “base period” of the AoA (i.e. the new agreement will take the “dirt” and the “water” out of the binding tariffs). If a reduction rule similar to that used in the Uruguay round is chosen, then higher percentage reductions might be agreed upon; if, on the contrary, the formula used determines a reduction of the higher tariffs by a larger percentage, then the overall average reduction will be lower. TRQs will likely be increased.

Export competition

Export subsidies will be further reduced based on a mechanism which will likely be not very different from that used in the AoA. Food aid, export credit policies and exporting STEs will be subject to somehow stricter and more effective rules (but the agreement will not go so far as to make export credits and trading by STEs subject to reduction commitments based on their export subsidy equivalent).

Other issues

Export limiting policies will either become illegal or subjected to strict rules. An agreement on the sensitive issue (not only for the EU) of the multilateral recognition of rules limiting the use of “denominations of origin” will be reached, but its content and effectiveness are hard to predict. On the contrary, it is unlikely that an agreement will be reached on allowing payments to farmers to compensate for stricter standards to protect animal welfare; this derives from the potentially far reaching consequences to other areas that such an agreement would have (different environmental standards and working conditions are the first to come to mind). Although “food safety” is among the issues to be addressed in the negotiations on agriculture, it is very unlikely that a meaningful and effective agreement will be reached on how to improve on the 1994 Agreement on Sanitary and Phytosanitary Measures to deal with the trade implications of different national food safety standards.

The main achievement of the 1994 AoA was “to bring agriculture into the GATT”, while its impact in terms of trade liberalisation remained fairly small; on the contrary, the new agreement will induce a significant liberalisation of agricultural trade, at least with respect to the distortions existing in the base period of the AoA (i.e. years 1986-88). However, it is hard to assess how much this liberalisation will be the result of the WTO agreement, and how much it will derive from policy reform processes autonomously decided by many of the countries whose policy interventions were distorting trade the most. Whatever the answer to this question, the new agreement will move the limits of what countries can do to support domestic agriculture further inward, making policy U-turns toward higher protection impossible in the future.

7 Concluding remarks

Although recent policy developments in the United States have seriously reduced the already relatively slim chances of a far reaching WTO agreement on agriculture, the outcome of the on-going negotiations is still likely to induce the need for significant adjustments in the CAP. This need is mainly limited to (a) changing the nature of direct payments to farmers to make them compatible with the new domestic support reduction commitments, and (b) reforming the CAP in those sectors where policy changes in the 90s were minor or nil (e.g. dairy products).

The policy changes which can be foreseen as a result of the likely ending of the WTO negotiations on agriculture seem to be compatible with what the EU has been saying it should do (but, so far, it has not been in a condition to do) to bring agricultural policies more into line with the role agriculture plays in EU society and economy today.

Moreover, policy changes which can be foreseen as a result of the likely conclusion of the WTO negotiations on agriculture seem to go in the same direction, but are of a much smaller order of magnitude, than those needed to make the current CAP financially compatible with the enlargement to Central and Eastern European Countries.