WTO Negotiations on Agriculture: Problems and Ways Ahead

"Background Briefing Paper for Session 1"

Kevin Watkins

Introduction

'We recognise the need for all peoples to benefit from the increased opportunities and welfare gains that the multilateral trading system generates.'
Ministerial Declaration, WTO, 14 November 2001

Three years on, the encouraging words adopted at the start of the Doha Round have a hollow ring. So far, the 'development' round has delivered little more than encouraging rhetoric, punctuated by deadlock and episodic breakdown. Rich countries have not delivered the reforms needed to make the global trading system a more powerful force for development. Failure to change this picture will inevitably damage the legitimacy of the rules-based system represented by the WTO, with attendant implications for multilateralism. There is a broad consensus that the costs of failure will be high. Can they be avoided?

The answer to this question will depend crucially on progress in the negotiations on agriculture. Reform of the rules governing agricultural trade is essential for both substantive and symbolic reasons. The substantive reasons are well known. Industrialised-country support programmes restrict access to Northern markets, generate large surpluses, and subsidise exports. Producers in developing countries – a constituency that includes a large proportion of the world's poorest people – are excluded from market opportunities and forced to compete against heavily subsidised competition in international and even in local markets.

The symbolic relevance of the negotiations on agriculture relates to the legitimacy of the WTO system itself. Most developing countries see a change in the rules on agriculture as a litmus test for the commitment of rich countries to a fairer international trading system. Notions of fairness may be disputed, but current agricultural rules and trade practices enshrine what can only be described as a set of double standards. Northern governments seldom miss an opportunity preach the virtues of openness to developing countries, while remaining resolutely protectionist themselves. Rules in the WTO perpetuate a system under which the distribution of opportunity in agricultural trade is shaped not by comparative advantage, but by comparative access to subsidies – an area in which rich countries have an unrivalled advantage. Failure to change this picture will inevitably reinforce a perception that WTO rules skew the benefits of trade and globalisation towards the industrialised world.

In an optimistic scenario, the Doha Round could still produce real change. In past WTO Rounds, agricultural trade negotiations were essentially a bilateral EU–US affair. Developing countries – the vast majority of WTO members, with the biggest stake in agricultural trade rules – were bystanders. Negotiating outcomes reflected inequalities in negotiating power. Thus the Uruguay Round Agreement on Agriculture (AoA) provided a multilateral façade for what was a bilateral arrangement designed to accommodate, rather than constrain, EU and US subsidies. The arrival of the G20 and the increased voice of African governments during the Cancun ministerial summit have fundamentally shifted the terms of engagement on agriculture, making a repeat performance of the Uruguay Round unlikely.

Prospects for a positive outcome have been strengthened by wider developments. Dispute-panel rulings have directly challenged EU and US agricultural support systems, creating precedents for future action and, by extension, incentives for northern governments to seek a rules-based resolution. With the expiry of the Peace Clause, Northern governments must now weigh consideration of WTO legality in the balance of domestic reform considerations.

Since Cancun, the WTO negotiating atmosphere has been characterised by rapid mood swings. The most recent swing appears favourable to a settlement, with the EU and the US adopting more conciliatory language. Having threatened a new wave of unilateralism and bilateralism, the US Trade Representative, Robert Zoellick, has recently indicated a strong preference for multilateralism – and a willingness to resume agricultural trade negotiations. The EU trade commissioner's recent offer to end export subsidies could be viewed, at least on a charitable interpretation, as another step in the right direction. On the other side of the equation, serious problems remain. It is one thing for outgoing trade representatives to hint at a new political dynamic. Converting broad pledges into fundamental reform of the 2002 Farm Act or the Common Agricultural Policy (CAP) is likely to prove a very different matter.

This paper looks at some of the issues at stake in the Doha Round negotiation on agriculture, and at strategies for achieving tangible outcomes that benefit developing countries. Ultimately, an agreement on agriculture is not an end in itself. It should be viewed as one of the means to the end of reforming the policies that cause global poverty. In strategic terms, we argue that stringent disciplines on direct and indirect export subsidies, and on the support systems that generate surpluses, should be the immediate priority.

Such disciplines will require a fundamental departure from the current negotiating framework – itself a product of the Uruguay Round. The distinction between 'distorting' and 'non-distorting' subsidies at the centre of this framework is unworkable and unwarranted. It has allowed the EU and the US, the architects of the framework, to evade disciplines on support and continue subsidising over-production on a business-as-usual basis. Subsidy segmentation is another problem. Domestic support and export subsidies are currently treated as separate categories, whereas their market effects clearly overlap. For example, all payments to sectors in structural surplus clearly incorporate an export subsidy component.

Special and differential treatment is another core theme in this paper. Failure to allow developing countries the policy space to protect their agricultural systems in the interests of food security would compromise efforts to combat rural poverty. Yet proposals tabled by northern governments advocate a restriction of this space through import liberalisation. Leaving aside the hypocrisy implicit in highly protectionist, heavily subsiding rich countries demanding market liberalisation in poor ones, liberalisation in agriculture has the potential to inflict grave human development costs. The key requirement for special and differential treatment is an acceptance that one size of agricultural agreement does not fit all – and that there should be limits to the reach of multilateral rules.

Such an outcome will be difficult to achieve. Increased access to developing country markets is one of the central pillars of agricultural policy in the US - and for reasons that are readily apparent. One consequence of the structural surplus built into US farm production is that access to foreign markets is vital: overall, exports account for one quarter of agricultural sales. In contrast to manufacturing, agriculture generates a large balance of payments surplus. Recent trade deals negotiated with the five countries of the Central American Free Trade Agreement (CAFTA), the Andean pact countries, and Australia, have served to highlight the mercantilist underpinning of US strategy, with a twin emphasis on aggressive market opening overseas and (witness sugar under CAFTA) limited market access at home. Strong special and differential treatment applied to a large group of developing countries would clearly rest uneasily with the commercial imperatives driving US policy - and it would provoke opposition from powerful domestic producer and agribusiness interests.

The G20 remains the alliance most likely to deliver an agreement that tackles the interlocking problems facing developing countries. However, it faces formidable challenges. The ultimate test for any coalition is not so much whether it advances shared interest, but the way in which it deals with differences and builds bridges to other alliances. Fault lines in the G20 are already clearly visible, not least to EU and US negotiators. Differences over preferences, the pace and scope of liberalisation, and over special and differential treatment all have the potential to cause conflict and to weaken the bargaining power of developing countries. However, the WTO is a vehicle through which developing countries can build pressure for the reform of policies that are detrimental to their interests, not to mention the interests of most people in industrialised countries.

This paper is organised as follows: Part 1 briefly summarises the problems associated with Northern agricultural policies. Part 2 turns to some of the issues raised by approaches to the measurement of agricultural support, focusing on the distinction between 'distorting' and 'non-distorting' subsidies. Part 3 considers the implications of some recent dispute-panel rulings. Part 4 examines issues at the heart of the debate on special and differential treatment. Part 5 concludes by reviewing some of the strategic choices facing developing countries.

1. Subsidising poverty: the impact of Northern agricultural policies on developing countries

Agricultural trade negotiations at the WTO are shrouded in a complex legal and technical discourse that sometimes obscures the importance of the underlying issues at stake. The outcome of these negotiations matters, because it will have an important bearing on the future distribution of benefits in international trade – and hence on patterns of globalisation. More immediately, changes in WTO rules will define the terms of competition between the highly capitalised, large-scale agricultural systems of industrialised countries on the one side, and the smallholder agricultural systems of poor countries on the other.

For producers in developing countries, the structure of this competition matters a great deal. Two-thirds of all people surviving on less than $1 a day – around 800 million in total – live in rural areas, most of them working as smallholder farmers and agricultural labourers. The profile of international poverty may be increasingly urban, but on current trends, the rural share of international poverty will remain above 50 per cent for the next thirty years. While the rural poor have diverse livelihood structures, they depend critically on income generated by the sale of farm products and on agricultural wages. Agricultural income growth also generates strong multiplier effects beyond agriculture. Research by the International Food Policy Research Institute (IFPRI) in sub-Saharan Africa suggests that every $1 generated in the agricultural sector can produce $3 through linkages to other sectors.
Such facts explain why, for a large group of developing countries, growth in agriculture – especially in the smallholder sector – will continue to have a disproportionate effect on poverty reduction.

It goes without saying that international trade is not the most important factor shaping prospects for rural poverty reduction. Export activity can benefit smallholder farmers under the right conditions, but those conditions – which include access to land, credit, and marketing infrastructure – are often lacking. This explains why agricultural export growth has been a more powerful force for poverty reduction in Vietnam than Brazil. Domestic policies, not WTO rules, hold the key to achieving a wider distribution of benefits from integration into global markets. However, WTO rules matter precisely they define the space in which domestic policies are formulated.

Overall agricultural support

Competition between Southern and Northern agricultural systems has a bearing on the markets in which many smallholders operate. The terms of that competition are largely dictated by the support systems operating in Northern agriculture. Measurement of this support is a controversial exercise – and as we show below, one that has a direct bearing on WTO negotiations.

Using the OECD's Producer Support Estimate (PSE), overall support for agriculture in industrialised countries amounted to $230bn in 2001, with the EU and the US accounting for two-thirds of the total. Support levels, as measured by the PSE, are equivalent to one third of the value of output in the EU, and to one fifth in the US. Beyond these broad headlines, there is ample scope for creative interpretation. Policy makers in the US point out that the EU has a higher overall level of support, and and that this support represents a higher share of the value of output. In retaliation, the EU likes to highlight the higher per capita support provided to US farmers. The more important point is that US support is more heavily concentrated on a narrow range of products, for which the US is a major exporter. As a consequence, US subsidies may distort key international markets more than is indicated by simple PSE comparisons.

Agricultural support in industrialised countries takes a bewildering variety of forms. Market-price support accounts for around two-thirds of the total, albeit with large variations between countries (the US is lower than the EU on this count). From an international trade perspective, OECD support is important for a number of reasons. The US is a major exporter of crops such as cereals, rice, and cotton. International markets absorb a large share of production for basic commodities such as wheat (45 per cent), soybeans (34 per cent) and rice (40 per cent). For its part, the EU is a major exporter of cereals, dairy, and sugar products. It follows that the terms on which the EU and the US produce and export have implications for the global market. At the same time, OECD support systems restrict the entry of imports through a complex array of tariff and quota arrangements.

Policy makers in the EU and the US regularly seek to justify agricultural support by reference to social equity objectives. In passing the 2002 Farm Act, President Bush appealed to a tradition of independent family farming, while the French agricultural minister has described the CAP as part of the EU social model. Back in the real world, agricultural subsidies are directed overwhelmingly towards large producers and agribusiness interests. The Gini coefficient for the distribution of agricultural subsidies is 77 for the EU and 79 for the US. For purpose of comparison, the Gini for Brazil is 60. Second-Round subsidy effects are also highly regressive, since they inflate land rents and prices for inputs. The point here is that current support patterns are bad not only for the poor in developing countries and for global income distribution, but also for distribution in subsidising countries.

Transmission effects

The overall effect of Northern agricultural support is an incentive structure that restricts imports, expands output, and generates large surpluses that are exported, usually with the help of a range of direct and indirect subsidies. Developing countries and their agricultural producers suffer the costs of this through four transmission channels:

- **Restricted market access** Tariffs and quotas create import-substitution effects in favour of producers in rich countries. Average tariffs understate real levels of protection for various reasons, including the large variance in tariff rates, the incidence of tariff peaks, and prevalence of specific duties. Even so, they are two to four times the level of average tariffs in manufacturing, with peaks up to 500 per cent. For the Quad group, around one third of tariff lines in agriculture carry applied rates in excess of 30 per cent. Northern market-access restrictions affect developing countries in various ways. Most obviously, they restrict imports: South–South agricultural trade has been growing at three times the rate of Southern exports to industrial countries. Growth rates in the latter area have been falling. Northern import restrictions also slow the rate of world trade growth in agriculture. Agricultural trade is growing at half the rate of manufacturing trade, and it is decelerating.
- **Lower world prices and increased price volatility** The scale of these effects is the subject of considerable controversy, partly because of the speculative nature of econometric modelling. For what they are worth, which may not be a great deal, the most widely cited models point to price increases in the range of one to ten per cent for grains, with higher levels for sugar and cotton. For the latter commodities, short-run price reduction effects are in the range 20 to 25 per cent. Other models contest these figures, predicting limited price adjustments associated with Northern support. Northern protection and support tends to increase price volatility because producers in OECD countries are in large measure insulated from price signals on international markets. For example, when

world cotton prices fell sharply in the second half of the 1990s, US producers continued to expand production and exports, transferring adjustment pressures to other suppliers.

- **Lost shares in world markets** Exports facilitated by subsidies artificially expand OECD market shares. In some sectors of concern to developing countries – including cotton, sugar, rice, and dairy – subsidized exporters are a major presence in the international market. Moreover, intra-industrial country trade still accounts for almost half of world agricultural trade, roughly the same levels as two decades ago.
- **Lower prices and displacement in domestic markets** Econometric models register a decline in import prices as a gain in consumer welfare. However, subsidised OECD exports can produce negative consequences for rural producers in the importing countries, both through displacement effects and as a result of lower prices. These market effects have in turn impacted on rural investment and wages. At a national level, export subsidies can have the effect of converting consumer tastes and creating a dependence on imports.

Economic modelling exercises have been widely used to measure the potential benefits of liberalisation. Most predict that rich country liberalisation would generate welfare gains for developing countries, ranging between $8bn in an IMF variant to $40bn in the International Food Policy Research Institute's general equilibrium model. These gains reflect adjustments in international prices and world market shares. Inevitably, global models reflect large aggregations that obscure regional and national differences, as well as distinctions between short-run and long-run effects. Major exporters stand to gain both from the higher prices and market share changes associated with liberalisation, while food importers are predicted to face higher import costs (and associated consumer welfare losses). Models tend to predict the largest gains for Latin America, with sub-Saharan Africa experiencing small gains or losses.

It has to be stressed that most modelling exercises incorporate heroically speculative assumptions about price and supply elasticities. This weakens their relevance to policy makers grappling with intense debates about the effects of even marginal policy realignments. So, too, does another consideration. Most modelling exercises point to relatively small aggregate gains for developing countries resulting from sweeping, and arguably implausible, liberalisation scenarios in industrialised countries. For example, the IMF model predicts that full agricultural policy liberalisation in industrialised countries would raise developing country GDP by 0.1 per cent - not a scenario likely to prompt urgent action on the part of G8 leaders.

None of this deflects from the real problems caused by industrial country policies. As with any large aggregation, net outcomes obscure problems facing countries in the sample – and some countries and groups of producers face very large losses indeed. In terms of foreign exchange costs, OECD support systems inflict the highest costs on major exporters. For example, Argentina loses heavily in the cereals sector, and EU sugar policies cost Brazil in excess of $400m annually. Countries such as Viet Nam and Thailand also suffer losses in exports of rice – a crop grown predominantly by small farmers.

Countries in sub-Saharan Africa are not immune to the effects of OECD policies. In the case of cotton, the region suffers both market displacement and price-reduction effects.

The background to this case is well known, but bears repetition. US support for its cotton producers in 2000/01 amounted to just under $4bn – an amount comparable to the market value of output. Because the US accounts for around one quarter of world exports of cotton, its domestic support has global market consequences. According to the International Cotton Advisory Committee, that support has lowered world prices by around one quarter. For countries such as Burkina Faso, Benin, and Mali, where cotton accounts for around one third of exports, the implied costs in terms of foreign exchange losses are very high; they are estimated at $200m for 2001. The impact on household income for the 10 to 11 million smallholders involved in growing cotton is more difficult to establish. However, household-income data for Benin suggests that the decline in the world price caused by US subsidies is correlated with a 12 per cent increase in poverty, pushing an additional 250,000 people below the national poverty line. To put US subsidies into perspective, they exceed the total GDP of countries like Burkina Faso and Mali.

Several case studies have highlighted the impact of subsidised Northern agricultural exports on local markets. During the 1990s, import liberalisation exposed agricultural producers in a growing number of developing countries to competition from subsidised imports. In Mexico, liberalisation under NAFTA has resulted in a sustained increase in imports of maize – a crop grown by around 2.4 million Mexican smallholder farmers. Agricultural policy makers in the US herald this as a triumph for market efficiency. But US maize growers received $6bn in direct payments in 2001, an amount equivalent to five times the federal agricultural budget for Mexico. Smallholder maize farmers in Mexico have suffered lower prices and market displacement.

In some cases, import liberalisation has led directly to a surge in heavily subsidised imports and attendant market disruption. This was the case in the rice sector in Haiti in 1995 (facilitated by IMF loan conditions requiring rapid import liberalisation) and in the Indian dairy sector in 1997. For a larger group of developing countries, imports have climbed steadily over time. The FAO estimates that food imports now account for 10 to 12 per cent of the calorific intake of Least Developed Countries, and that the food-import bill now represents over three per cent of their GDP. While the underlying causes of this increase in dependence on food imports are complex and varied, the disincentives for local investment created by export subsidies are a factor of considerable importance. In terms of food security, the chronic balance-of-payments problems facing a number of low-income countries makes them highly vulnerable to risks associated with periods of high prices.

Trade preferences

Trade preferences add another dimension of complexity to North–South agricultural trade relations. Tariffs and quotas introduce a wedge between world prices and OECD domestic prices. In principle, preferential schemes allow suppliers in beneficiary countries to access part of the price premium, effectively raising the rate of return on investment. In practice, the benefits of preferences are diminished through complex entry systems and eligibility requirements.

Some of the problems are well known. Under many schemes – such as AGOA – preferences can be withdrawn at any time. Product coverage is often limited, as reflected in regional trade agreements. Mercosur exporters face agricultural tariffs in the EU that are 50 per cent higher than those faced by the EU in its exports to countries in the group. Preferences over MFN rates are minimal. As in other arrangements, the EU prefers to concentrate its preferences on products that it does not produce - or on countries that lack the capacity to take advantage of market opportunities. Regulations concerning the origin of items eligible for preferences are another factor limiting the ability of would-be suppliers to fill quotas. An additional problem is that preferences can lock countries into production in areas where they have limited comparative advantage, exposing them to future risks.

Such considerations have prompted the World Bank and others to take a dim view of preferential trade. There is no shortage of economic models purporting to show that, in aggregate and over the long-run, preferences hurt their putative beneficiaries. Not surprisingly, the beneficiaries themselves take a different view. African and Caribbean exporters of sugar to the EU receive a price some three times above the average world market price for a fixed quota of sugar. In the absence of preferences, many sugar industries would either contract or collapse. Similarly, tariff preferences under the EU Cotonou agreement provide important advantages to Africa. Governments in the region see the agreement as vital to protection against competition from Latin America. For negotiators representing countries with preferences at the WTO, preference erosion can pose a real and immediate threat to export markets. That threat is likely to weigh more heavily in the design of trade policy than the results of economic modelling exercises.

2. Measuring support under the Agreement on Agriculture

Prior to the Uruguay Round, multilateral rules were of limited relevance to agricultural trade. The Agreement on Agriculture (AoA) started to change this picture, introducing for the first time a framework of rules and disciplines to limit support. The Doha Round negotiations operate within the parameters of the AoA. Unfortunately, this starting point severely disadvantages developing countries.

The AoA suffers from two fundamental flaws. First, it is enshrines an arbitrary distinction between 'distorting' and 'non-distorting' support. Initially developed under the Blair House accord between the EU and the US, this distinction has enabled the subsidy superpowers to evade disciplines on supports that damage developing country interests. The second, more fundamental, problem can be traced to the tripartite structure of the AoA framework. Under this framework, domestic support, export subsidies, and market access are treated as segmented units. This is unfortunate, because the distinction between export subsidies and domestic supports is increasingly blurred.

When is a subsidy not a subsidy?

The mandate of the Doha Round mirrors the provisions of the AoA. Governments are expected to deliver the following outcomes:

- ‘Substantial reductions of trade distorting **domestic support’**
- ‘Reductions of, with a view to phasing out, all forms of **export subsidies**’
- ‘Substantial improvements in **market access**’

The term 'trade distorting' is of more than passing relevance in application to domestic support. Earlier we used the PSE as an indicator of overall levels of support to OECD agriculture. For the purposes of WTO negotiations, a different measure is used: the Aggregate Measure of Support (AMS). In nominal terms, the AMS is supposed to capture 'trade distorting' subsidies. Under the AoA, a ceiling is set in AMS terms at $21bn for the US and $19.8bn for the EU.

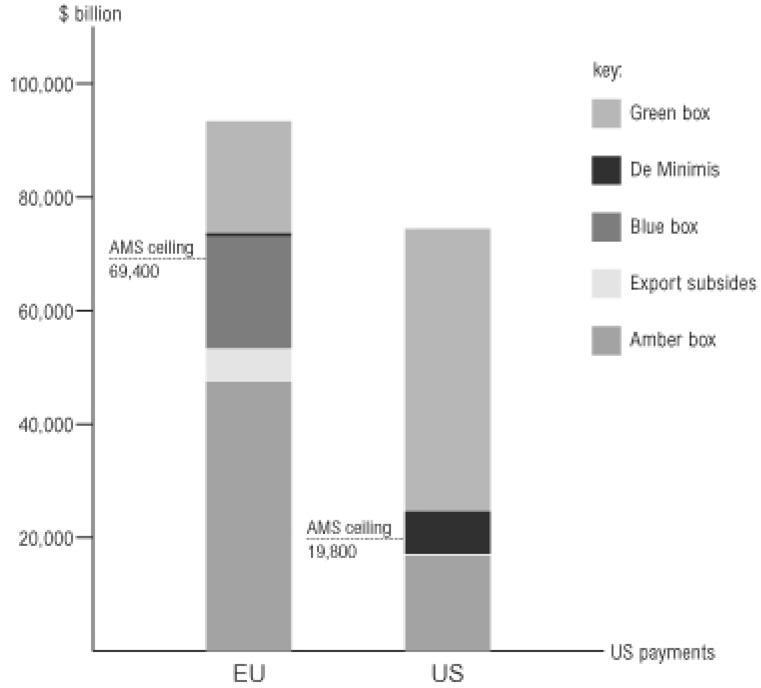
The subsidy 'box' system is supposed to reflect the differentiation of subsidies. All domestic-support measures deemed to distort production and trade fall into the ‘Amber Box’. Under the Uruguay Round AoA, these are subsidies that have to be cut, subject to a provision known as the 'de minimis' arrangement. Under the terms of the latter, Northern governments can provide financing up to the equivalent of five per cent of the value of production (the figure is 10 per cent for developing countries). Export subsidies also fit into the category of AMS support, subject to limits and reductions. Under the terms of the Uruguay Round, the EU and the US are required to keep the AMS below a specified ceiling. The rate at which the ceiling is lowered in the years ahead will depend on the outcome of the Doha Round negotiations.

The ‘Blue Box’ can be thought of as the Amber Box with conditions. Support that would normally be placed in the Amber Box can be placed in the Blue Box if it is linked to a programme designed to limit production. An example of such a programme is the EU's set-aside arrangement, first introduced under the 1992 reforms. There are no limits on the amount of support that can be provided under the Blue Box – an issue that figures prominently in current negotiations.

The ‘Green Box’ is defined in Annex 2 of the AoA. In order to qualify for this category, subsidies should either not distort trade at all, or cause minimal distortion. Green Box subsidies can be provided without limit.

What is the relevance of all this for negotiations to change Northern agricultural policies that cause over-production and facilitate export subsidisation? **Figure 1** offers a partial answer. It provides a breakdown of support categories for the EU and the US for the marketing year 1999, the last year for which official reports are available.

Figure 1 EU and US support by WTO reporting category (1999)
Source WTO



Source: WTO

What emerges from the data is that the EU and the US have complied with the letter of the AoA. In 1999, both were operating well within the bounds of their AMS ceilings. For the EU, combined Amber Box and export subsidies represented 76 per cent of the AMS ceiling, rising to 84 per cent for the US. However, Figure 1 also demonstrates that compliance with the AoA has been achieved through a process of subsidy shifting, or the transfer of support into the Green Box and the Blue Box. In the case of the US, supports subject to WTO disciplines represented only 22 per cent of overall support, rising to 69 per cent for the EU. For developing countries concerned with the trade distorting effects of agricultural support, this raises an obvious question: namely, are the non-disciplined supports genuinely non-distorting?

The current state of research does not allow this question to be answered with any accuracy. Financial transfers linked to historic production levels rather than current output (one of the criteria used for decoupled payments) provide capital and an increased level of security against risks posed by price fluctuations. To the extent that payments are linked to land, they inflate land values and hence borrowing capacity. By contrast, other transfers linked to environmental policy goals may have far weaker market effects. Unfortunately, the current system of categorisation, delays in EU and US reporting to the WTO, and the limited relevance of either the AMS or the PSE as indicators, leaves developing countries with limited leverage beyond the dispute settlement system for challenging northern government practices.

Domestic policy reform agendas

Agreements at the WTO reflect a dynamic interaction between domestic reform strategies and trade negotiations. There are complex feedback loops connecting positions adopted at the WTO and the development of domestic policies. Nowhere is this process more evident than in agriculture. Domestic policies are contested by powerful interest groups, many of which operate through political associations structured around the maintenance of access to subsidies and rent-seeking. Northern governments are inevitably constrained by the effectiveness of these associations. At the same time, they have to balance wider objectives – such as agreements in non-agricultural areas and the development of the WTO system itself – against the claims of vested interest groups.

The imprint of domestic policies on WTO agreements is much in evidence, notably with regard to US policies. At the time of the Uruguay Round, a large share of US support was directed towards programmes incorporating (largely unsuccessful) supply management requirements. The 1992 CAP reforms took the EU in the same direction. Both parties had an interest in a provision that maximised flexibility in this area and minimised multilateral constraints – hence the Blue Box. Having moved towards more 'decoupled' payments – a process that gathered pace with the 1996 Federal Agricultural Improvement Act (FAIR) – the US had an interest in even weaker disciplines in this area, which were duly catered for with the Green Box.

The important point here is that subsidy re-ordering and reclassification enabled the EU and the US to make deep cuts in their respective AMS levels with minimal adjustment. Measured by reference to the PSE, both parties *increased* support between 1986-1998 (the reference period for Uruguay Round subsidy reduction) and 2000. When it comes to agricultural negotiations in the WTO, measurement matters a great deal. Beyond the complex technical problems involved, developing countries have a strong interest in preventing a Doha round outcome that accommodates another bout of subsidy repackaging. This in turn will require an understanding of how the parameters of domestic reform debates in the EU and the US play out at the WTO.

The current direction of reform poses both threats and opportunities. In the case of the US, the 2002 Farm Act accelerates a move back from the decoupling model adopted in 1996. The move started with the expansion of 'emergency payments' and an increase in market-price support payments in response to low world prices at the end of the 1990s. Non-decoupled output-based payments increased from \$1.6bn annually for 1996–98 to \$9bn in 1999–2001. The 2002 Farm Act legislation increases loan rates (in effect, minimum guaranteed prices), updates the acreage and yields on which direct payments are based, and institutionalises a system of counter-cyclical payments. One upshot is that the US is now almost certainly pushing close to its AMS ceiling, creating strong incentives to either limit ceiling reductions and weaken disciplines on direct payments.

Just how close the US is to the ceiling is uncertain, since the status of many of these payments remains uncertain. The structure of payments for 2003 in summarised in **Figure 2**. An immediate problem for policy makers in the US is that the 2002 Farm Act may have been leveraged previously Green Box support into the Amber Box, in which case their ceiling has already been exceeded. Even before the new legislation, low world prices were pushing the US closer to its AMS ceiling. Were prices to fall again, the provisions of the 2002 Farm Act would almost certainly generate support levels above the ceiling. Apart from restricting the room for manoeuvre, this implies that an agreement at the WTO will require major legislative reform in Congress. US negotiators at the WTO are likely to seek a high level of flexibility in the definition of the Green Box and to keep open the possibility of recourse to the Blue Box, possibly with reference to counter-cyclical payments.

Figure 2 US direct payments to agriculture (2003)

Source: USDA, commodity credit corporation

In the EU, the ambition of CAP reformers has been to shift support into the Green Box through full decoupling. Differences between member States have limited progress, resulting in a (very) partial decoupling under the June 2003 reforms. Meanwhile, one major sector – sugar – is as yet unreformed. Translated into WTO strategy, the parameters of CAP reform dictate that the EU is likely to drive a hard bargain in seeking to maintain the Blue Box and a residual right to subsidise directly exports in key sectors.

Any agreement in the Doha round will incorporate provisions for 'decoupled' support – and rightly so. It would be politically unrealistic and socially undesirable to argue for the elimination of northern government support in area where there is a clear public policy interest. For developing countries the key question is what constitutes 'decoupled' support and, by extension, what is eligible for the Green Box. This is an area in which more research and a better understanding of the market effects of policies is vital. What is clear, however, is that much of the support currently directed into the Green Box does damage the interests of developing countries.

Export subsidies and export dumping

From the perspective of developing countries, and – more importantly – their agricultural producers, the classification of subsidies at the WTO is of less relevance than their effects on markets. Export subsidies represent a major source of concern, since they are widely regarded as being among the most damaging. With the shift in structure of Northern support, the distinction between export subsidies and domestic support is becoming increasingly artificial.

This problem can be demonstrated by reference to Figure 1, which shows that, for the purposes of WTO classification, the US was a non-subsidising exporter at the end of the 1990s – and this remains the case. The EU accounted for over 90 per cent of OECD export subsidies in 1999. However, even then they represented a relatively small component of overall support; and that component has been shrinking since 1999. Cuts in guaranteed domestic prices allied to increases in world prices have enabled the EU to export at prices above domestic levels. Only two major sectors – sugar and dairy – now consistently depend on direct export subsidies.

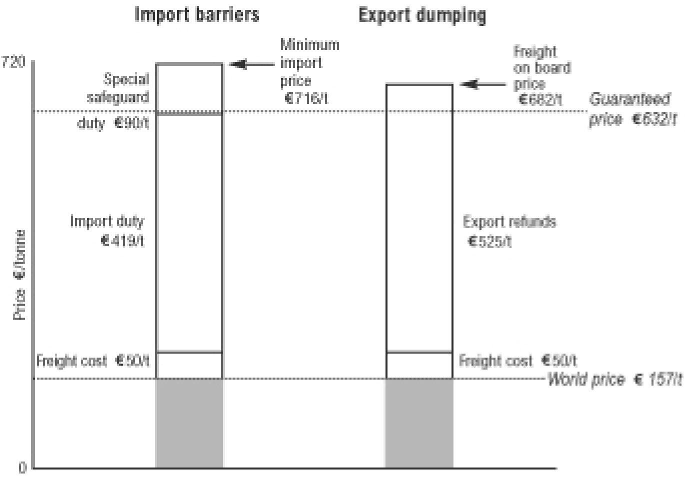
The word 'direct' is operative in this context. Both the US and the EU provide very high levels of support to sectors that are in structural surplus. Indeed, in many sectors, these surpluses would not exist in the absence of direct payments to farmers. It follows that direct payments include a *de facto* export subsidy, even though they are not reported as such *de jure* for WTO purposes.

The problem can best be demonstrated by reference to specific commodities. Mention has already been made of the $4bn in direct payments allocated to cotton producers. In terms of WTO reporting, only around two per cent of these payments can be categorised as export subsidies. Yet in the absence of direct payments, US export activity in cotton would be much diminished for an obvious reason: in most years average production costs considerably exceed world prices. Under non-subsidised conditions, cotton would not be a profitable crop for the vast majority of US producers. Cotton is not unique. In the case of rice, the OECD estimates US support to be equivalent to just under half of the value of output. Around one third of production is exported, again without the help of export subsidies. Similar conditions prevail in maize and wheat. The point in all of these cases is that direct payments clearly spill over into export subsidies, though they are treated purely as domestic supports for WTO purposes.

In the interests of balance, it has to be acknowledged that the hidden export subsidies at work in the EU are on a larger scale than those applied in the US. One way of capturing this scale is to adopt the simple expedient of dividing the volume of output in any sector by the value of direct payments. This creates a unit value of subsidy measure, which can in turn by converted into an export subsidy by reference to export volume. On this measure, the EU provides an export subsidy of around $610m for 2001. However, no official export subsidies were recorded in this year, underlining the limited nature of the current reporting regime.

The sugar sector in the EU provides an even more telling example. Europe is the world's second largest exporter of sugar after Brazil, supplying around five million tonnes annually to the world market. These exports are sustained on an annual basis, even though guaranteed prices under the CAP are some four times world market prices (**Figure 3**). As the EU's own Court of Auditors has acknowledged, there would be no European sugar exports in the absence of subsidies. Yet the EU admits to subsidising around one half of total exports. It maintains that the other half is non-subsidised or, more accurately, 'self-financed' through a levy paid by producers – an argument now under challenge in a WTO dispute panel (see below).

Figure 3 The CAP sugar regime in operation: import barriers and export subsidies (2004 prices)



Source: Based on data from International Sugar Organisation and European Commission

The Institute for Agriculture and Trade Policy (ITAP) and others have helped to highlight the problem by focusing on the gap between export prices and cost of production. Under WTO rules, dumping is broadly defined as the sale overseas of a product at prices below the normal price prevailing on the domestic market. However, in cases where 'normal price' is impossible to establish, importers can construct value on the basis of cost-of-production criteria. Using these criteria, it is clear that the US is dumping without export subsidies on a large scale: export prices for cotton and wheat in 2003 were respectively around 50 per cent and 20 per cent of average production costs. In the case of EU sugar, the dumping margin measured as the gap between production costs and export price would be in the range 300–350 per cent.

Were the Indian textiles industry to attempt exporting to the EU or the US on similar terms, it could confidently predict a swift response in the form of a barrage of anti-dumping actions. Yet when it comes to agriculture, WTO rules allow the EU and the US to dump with something close to impunity.

Existing rules on export subsidies suffer from limitations in two further areas. First, they do not cover export-credit programmes – the principle form of direct export subsidisation in the US. While the EU accounts for the bulk of direct export subsidies, the US accounts for the lion's share of export credits. The GSM 102 and the GSM 103 programmes and the Supplier Credit Programme provide for financing of around \$5.5bn. These programmes are explicitly aimed at creating and maintaining commercial market outlets for US surpluses. They are extensively deployed in countries ranging from the Philippines to Mexico and West Africa. Depending on the method used to calculate concessionality, the subsidy component of these programmes is between $500m and $700m annually. The only international rules in operation are a set of best-endeavour clauses in what are largely unobserved OECD guidelines.

The second gap in WTO rules relates to food aid. US food aid programmes have developed in large measure as a surplus-disposal policy, geared towards the creation of commercial markets. This remains one of the core objectives of Title 1 of PL 480, under which eligible countries must 'demonstrate the potential to become commercial markets for US agricultural commodities'. The commercialised nature of Title 1 is apparent at a number of levels. Countries facing genuine food emergencies in southern and eastern Africa consistently receive less than do commercial market outlets. Moreover, US food aid transfers fall when world prices rise – the opposite of what might be expected under a demand-driven programme. Current budget authorisations for Title 1 amount to $176m annually, much of which could be categorised as export subsidies. For example, in 2001, Archer Daniel Midland, one of the world's largest grain traders, was awarded $35m in Title 1 contracts to supply corn and rice to the Philippines.

Market access

Negotiations on market access represent the third pillar of the Doha mandate. Once again, the shadow of the Uruguay Round looms large. The agreement reached was designed to facilitate evasion and limit adjustment costs on the part of industrialised countries. One of the central concerns for developing countries is to avoid a repeat performance.

Under the AoA, governments were required to reduce average tariffs on a linear basis – the so-called Uruguay Round formula. The aggregate nature of the tariff-cutting formula gave countries a great deal of flexibility. Large tariff reductions for commodities representing a small share of trade could be used to facilitate far shallower tariff cuts for commodities representing a larger share of trade. In fact, the high tariffs in operation during the reference years enabled most countries to meet their AoA commitments without difficulty.

In the Doha Round, debate has centred on the formula to be used for cutting tariffs. The 'friends of the Uruguay Round formula' group – which includes the EU, prefers a linear approach. Most developing countries – backed, with some reservations, by the US – want to have tariff cuts that escalate with the size of the initial tariff; the Swiss formula approach, as it is known. The aim is to create tariff convergence at a relatively low level, and to eliminate tariff peaks.

Most formulae envisaged for the Doha Round are a blend of the two approaches. As expressed in the Derbez text (the last under consideration before the collapse of the Cancun summit) this would segregate tariffs into three groups. For one, average tariff cuts would be applied with a minimum for each tariff line. For another, higher tariffs would be lowered proportionately more than lower tariffs, and a tariff ceiling would be applied; remaining tariffs would be eliminated. The progressivity of the reduction would be determined by a coefficient. For the final group in the Derbez proposal, tariffs would be eliminated.

The broad consensus is that a cocktail approach is needed. Beyond this starting point, there are deep divisions. One of the problems with the Derbez text is that it leaves room for creative evasion. Northern governments could apply the Swiss formula on tariffs that are already relatively low, and the linear Uruguay Round formula for higher tariffs, creating ample scope for the maintenance of tariff peaks. [*These issues are dealt with in more detail in the background paper by Panos Konandreas.]*

3. WTO dispute-panel rulings

WTO case law has become an increasingly important factor in shaping the negotiating environment. With the expiry of the Peace Clause, principles established in dispute-panel rulings now constrain the options open to Northern policy makers in agriculture – and they could strengthen the hands of developing country negotiators. Three such cases merit special attention.

The Brazil–US cotton ruling The interim report on the ruling has not yet been made public. However, some of the decisions are now well known. Perhaps the most important is that Production Flexibility Contract support and, by extension, Direct Payments are non-Green Box, and therefore not exempt from subsidy reductions. It may well be that, if applied to other sectors, the ruling would place the US in breach of its AMS ceiling. Whether or not this is the case, the US is now highly vulnerable to dispute cases in other areas, even for periods covered by the Peace Clause. The Panel decided that US subsidies could not benefit from Peace Clause protection on the grounds that the level of support exceeded the amount provided in the base year. With regard to export subsidies, the Panel found against the US on two counts. First, it has ruled that a cotton-specific credit programme – the Step 2 programme – constitutes a prohibited subsidy. Second, and more importantly, it has ruled that the GSM and other export-credit programmes circumvent US export-subsidy commitment not just in cotton, but also in soybeans, fruit and vegetables, and rice. Finally, the Panel has ruled that US cotton subsidies cause significant price depression in world markets and in the Brazilian market. For various technical reasons, the Panel found against the claims that (i) US subsidies artificially increase US world market share and (ii) that subsidies enable the US to capture an inequitable market share (in the sense stipulated in the GATT Article XV1 subsidy code).

The Brazil, Thailand, Australia–EU sugar dispute Behind the legal complexities of this case, the central issue at stake is the definition of an export subsidy. The EU claims that two categories of its sugar exports are non-subsidised. Under the first category are the 1.2m tonnes exported through a levy on guaranteed prices paid to processors. In the view of the EU, the levy makes the exports 'self-financing'. Viewed from a different perspective, the levy itself is a mechanism for diverting part of a consumer transfer to the industry into a disguised export subsidy. Such arrangements are prohibited under Article 9 of the AoA – and the EU has put up at best a weak defence in the dispute panel. The second category of exports concerns non-quota sugar, or production that is not subject to price support. In effect, these exports are financed through a cross-subsidy from quota sugar. Support prices for quota sugar make it possible for producers to cover their fixed costs, with world prices covering marginal costs. The Court of Auditors of the EU has conceded that exports of non-subsidised sugar would not be feasible with a transfer of subsidies from quota sugar. If the EU loses the case at the WTO, it will recast the entire CAP reform debate as it relates to sugar, and raise questions about cross-subsidies in other sectors.

Canadian dairy dispute This case has set a precedent of direct relevance to the EU sugar sector. In it, the Dispute Panel ruled that domestic support applied to products in surplus can have the same effects as export subsidies. To cite part of the report, ‘We consider that the distinction between domestic support and export subsidy disciplines would be eroded if WTO members were entitled to use domestic support without limit to provide support for exports.’ This would appear to create a precedent for the EU sugar case. More generally, as with the Brazil–US cotton rulings, a WTO Dispute Panel has, in effect, challenged some of the central assumptions underpinning the AoA.

4. Special and differential treatment

The Doha mandate clearly establishes special and differential treatment as a priority for the WTO trade round. In the Derbez text, this is interpreted on the model established in the Uruguay Round, namely, 'same direction, different speed'. In agriculture, as in other areas, developing countries are broadly expected to follow the same reform path as industrialised countries, but over a longer time-frame, with shallower tariff cuts and exemptions for some forms of support from reduction commitments. However, the critical importance of agriculture to food security and poverty reduction raises important questions about the role and scope of WTO rules.

Market access

Much of the debate on special and differential treatment in agriculture has focused on the theme of market access. The approaches adopted by different governments serve to illustrate the complexities of the issues at stake, not least for the G20 group.

In the strategic vision of US negotiators, the aim of the Doha Round is to advance an aggressive movement towards trade liberalisation that extends beyond the borders of developed countries. To cite the letter of Robert Zoellick, the US Trade Representative, to trade ministers in January 2004: ‘For the United States, the degree of ambition is linked to ... a substantial increase in real market access opportunities both in developed and major developing country markets.’ Application of the Swiss formula, in the US view, should not be limited to industrialised country agriculture.

The US emphasis on market opening at the WTO is a multilateral extension of a wider strategic vision for agriculture. Mention has already been made of the acute dependence of US farm incomes on access to overseas markets. Beyond the farm sector, agricultural exports play a critical macro-economic role. The $10-20bn annual surplus posted on agricultural trade helps to offset deficits in other areas. As even a cursory tour of the USTR web-site will demonstrate, policy makers regard increased access to developing country markets as a vital objective.

In this context, NAFTA is held up as something of a model. Import liberalisation in Mexico led to an eighteen-fold increase in US maize exports from 1993-2000, with the overall value of agricultural exports doubling. The recently negotiated agreement with the five CAFTA countries (Costa Rica, Guatemala, El Salvador, Honduras, and

Nicaragua) provides for extensive market opening opportunities, with more than half of US agricultural exports now entering markets duty free and a fifteen-ear phase-out period for remaining tariffs. On the import side, Congressional opposition has limited US concessions. Both under CAFTA and the bilateral agreement with Australia, the US has maintained stringent import quotas on products such as sugar, beef and dairy, and prohibitive tariffs above quota. When it comes to agricultural trade, mercantilism is alive, well, and kicking in the US.

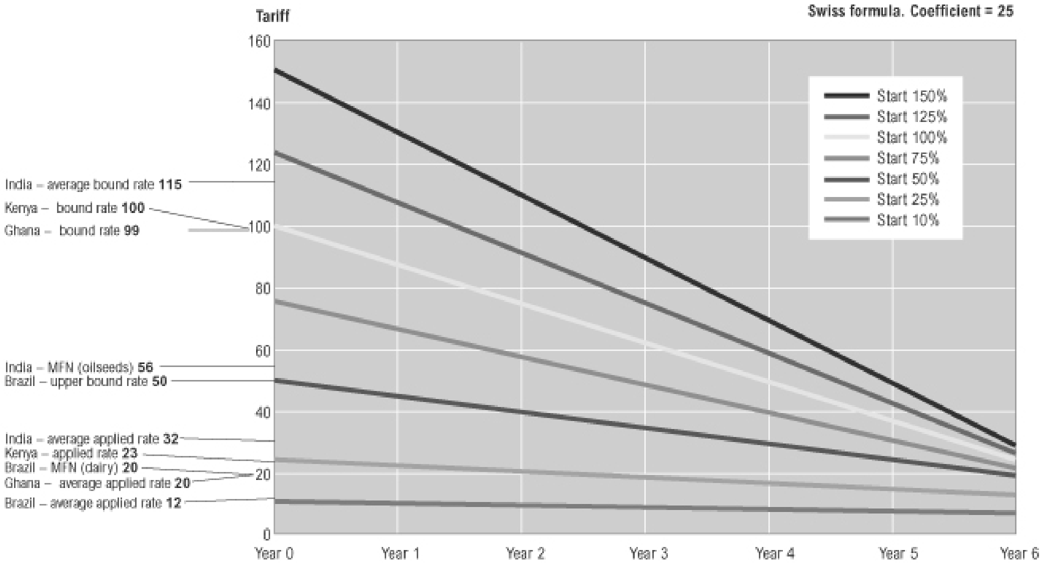
The form taken by this mercantilism has direct implications for special and differential treatment. Implicit in the USTR's formulation is a distinction between countries that represent major commercial markets and the rest – a radical new approach to the classification of developing countries for purposes of special and differential treatment. It might not unreasonably be assumed that the 'major market' group extends from low-income countries (including India and China), to middle-income countries (including Brazil and other Latin American countries, much of North Africa, and south-east Asia), and a large group of food importing developing countries. This is precisely the constituency that the US Department of Agriculture is anxious to cultivate for commercial market development.

Some support for the US view has come from other sources. The World Bank has argued that developing countries should accept the case for import liberalisation in agriculture, while acknowledging that institutional constraints may undermine the benefits of openness in low-income countries. Like the US, the Bank argues for greater differentiation between countries. Middle-income countries, so the argument runs, need to accept less protection and weaker special and differential treatment provisions. With two major exceptions, low-income countries would enjoy a higher order of special and differential treatment. The two exceptions in question are India and China, apparently on the basis of market size and what the World Bank sees as WTO *realpolitik* – a euphemism, in this context, for what is acceptable to the EU and the US.

It has to be emphasised that the debate over special and differential treatment raises matters of fundamental importance for agricultural trade policy formulation in developing countries. Nowhere is this more apparent than with regard to market access. Application of the Swiss formula to developing countries, as envisaged by the US, would entail very deep tariff cuts, implying potentially large shifts in relative prices between imports and domestically produced goods. The aim of the Swiss formula is to produce a narrow range of final tariffs from a wide set of initial tariffs, and to arrive at a tariff ceiling. The rate of convergence is decided by the coefficient used in the formula – a subject of intense controversy.[1] Figure 4 provides one possible scenario, using a Swiss-formula coefficient of 25. It shows that countries such as India would be faced with considerable adjustments.

[1] The Swiss formula is as follows $Z = CX/C+X$. Where Z equals the final tariff, X the initial tariff, and C the coefficient.

Figure 4 Application of the Swiss formula for tariff reductions



Source: WTO

Figure 4 also draws attention to another important aspect of the debate on market access as it relates to special and differential treatment: the gap between bound tariffs (the legally binding ceiling in WTO schedules) and applied tariffs (the tariffs that governments actually charge). For some developing countries, this gap is relatively large. If the benchmark for tariff cuts is the bound rate, this offers some flexibility – especially if countries have bound at high levels. However, one country – the US – has argued that negotiations to lower tariffs should start from applied tariffs, breaking with the tradition of all previous rounds. Wherever the benchmark is set, some countries will face acute problems. This includes those (such as Brazil, Peru, the Philippines, and Egypt) that have bound tariffs at relatively low levels, especially where bound rates are close to applied rates.

Special safeguards and special products

Various options have been advanced by developing countries, non-government organisations, and others concerned about the implications of import liberalisation in agriculture. These options include the application of special products and differential treatment for 'special products'. The aim is to reverse the erosion of special and differential treatment, and to address a broader set of concerns about food security.

Special safeguards Under Article XIX of the GATT, safeguards can be introduced as a temporary measure, following cuts in tariffs in response to import surges. Importantly, tariff reductions can only be reversed if it can be established that imports cause, or threaten to cause, injury to domestic producers. Provisions under the 'sunset' clause restrict the use of a safeguard to four years. As an instrument for protecting and advancing food security in developing countries, the safeguard arrangements suffer from a number of problems. These relate to capacity, notably with regard to establishing serious injury, cost of litigation, and time-horizon. Recourse to Article XIX is feasible for commercial agribusiness interests (domestic and foreign-owned), operating in developing countries. But it is of limited use as a support mechanism for public policies on food security.

The Uruguay Round did in fact introduce a special safeguard on agriculture, largely at the behest of industrialised countries. Under the AoA (Article 7), some member governments gained the right to impose additional tariffs in the event of an import surge. What differentiates the special safeguard from Article XIX is the application of automatic volume and price triggers. That is, the safeguard can be invoked in the event of specified shifts in import quantity and price, without demonstrating serious injury.

The current special safeguard suffers from two defects with regard to food security. First, like Article XIX, it is a temporary arrangement; additional duties apply for only one year, or for a specific shipment. Second, the provision is available only to countries that undertook tariffication during the Uruguay Round – a provision that excludes a large group of developing countries and product groups. Developed countries account for about half of the 6156 special safeguards on agriculture (the EU alone for 539).

Conditions for the implementation of a food security-focused special safeguard have yet to be spelled out. However, the broad idea is that the safeguard would retain the automaticity of the current arrangement, with a longer time-horizon and comprehensive developing-country coverage.

Special products The concept of special products has emerged as a second, related strand of thinking about special and differential treatment. Broadly, the idea is to identify products of critical relevance to food security and the livelihoods of the rural poor. These products would then either be exempt from cuts in tariffs and support, or subject to less stringent disciplines. Special safeguard provisions would also be tailored towards the special products. Various approaches have been proposed. Under the first Harbinson proposals, a simple linear average of 10 per cent was applied to tariff cuts for commodities stipulated in tariff schedules as special products, providing a waiver from the wider tariff-cutting formula. The same products would also be automatically eligible for coverage under the special safeguard.

Several governments and non-government organisations have set out broader proposals for a 'Development Box' in agriculture. The motivation behind these proposals is a concern to limit the scope of any WTO agreement in matters concerning food security. National sovereignty would hold sway over multilateral obligations. Thus a 'Development Box' provision would allow countries to raise tariffs on food security crops for which tariff bindings are deemed too low, regardless of tariff-cutting formulae.

Neither the US nor the EU have ruled out special-product or safeguard arrangements. However, their current negotiating strategies would aim to achieve a trade off between coverage and provision; that is, the wider the coverage, the weaker the provision. In other words, it is unlikely that industrialised countries will look favourably at a Brazilian request for treatment comparable to that provided for Africa.

Food security implications

The issues raised in the debate on special and differential treatment are of fundamental importance for rural development policies, poverty reduction, and food security. Unfortunately, the debate itself has been driven by a perverse logic. This is an area in multilateral obligations should be tailored to national poverty-reduction plans. Instead, negotiations over WTO rules, driven by the concerns of industrial countries to expand market access, are defining what is possible in national poverty planning.

International trade rules are only one factor affecting food security outcomes and the interaction between the two is complex. Food security is not the same as food self-sufficiency – as witnessed by the prevalence of malnutrition in India and Brazil. However, national self-sufficiency can be an important factor, especially in low-income countries. At a household level, food security is related to the ability to command access to nutrition on a sustainable basis, either through production or exchange. Agricultural protection is not inherently good for food security, either at a national or at a household level; as in the EU and the US, the benefits can be captured by the wealthy at the expense of the poor. By the same token, open markets and import liberalisation can undermine food security, as witnessed by the experience of a large number of countries.

The important point here is that there is no trade-policy blueprint for advancing food security interests. Demands tabled by industrialised countries may cite a food security rationale, but this is invariably a smokescreen for advancing the interests of commercial agricultural exporters. Consider the rationale advanced by the US and the World Bank for greater differentiation between developing countries. Headline distinctions between, say, India and Brazil on the one side and Burkina Faso on the other, have an intuitive appeal. India is a large country, and Brazil is the world's fourth largest agricultural exporter. Viewed from a food security perspective, the distinctions appear less well grounded. According to the World Bank, around 16 million Brazilians are affected by malnutrition, and there is a high incidence of poverty among smallholder farmers producing basic grains and other food crops. In the case of India, market size is not an antidote for rural poverty. More than three-quarters of India's poor – some 200 million people – live in rural areas, many of which do not figure in the 'shining India' growth model.

If one of the aims of special and differential treatment in agriculture is to create a national policy space to address food security problems, the rationale for excluding India and Brazil is not obvious. The same applies to China. After all, the food security problems facing the north-east of Brazil, the 'poverty belt' in northern India, and the interior of China are not diminished by export success.

Developing countries have responded to US and EU demands with an essentially defensive strategy focused on safeguards and special products. There are problems with this approach. The special safeguard is an instruments geared towards dealing with import surges, not with a sustained and regular increase in imports. Bound tariff systems lack the flexibility to respond to surges caused by large and unpredictable fluctuations in exchange rates, the gyrations in global market prices linked to changing supply and demand patterns in major markets, and, of course, northern subsidies. However, for countries seeking the policy space to reverse long-run, structural losses of food self-reliance in the interests of food security, rural development, and poverty reduction, the problem goes beyond anti-surge mechanisms. While protection is manifestly not a guaranteed route to food security, let alone an indicator of policies that support the rural poor, there may be strong infant industry and wider grounds for border protection to create incentives for local production and investment.

Some commentators argue that a special product provision could provide a framework for addressing this problem. The argument is that products with a direct bearing on food security would be accorded a different status. However, this approach is not without problems. There is an immediately obvious sense in which, say, Cambodian rice or Ghanaian cassava might be construed as food security crops, meriting different treatment. But as the Government of India has pointed out, palm oil, rubber, and cotton are also food security crops. Markets for these crops play a pivotal role in the lives of millions of small farmers and rural labourers. In most developing countries, the poor are involved in the production a wide range of crops and a combination of on-farm and off-farm employment. Simplistic distinctions between 'subsistence food crops' on the one side and 'cash crops' on the other do not help. As is now widely recognised, successful rural development and poverty-reduction strategies have to start out by developing policy frameworks that reflect the realities of these livelihoods.

The danger is that a compartmentalised, special-product negotiating strategy at the WTO will leave a large gap between the behind-the-border dictates of multilateral rules and the policy requirements for rural development. Developing countries face the prospect of being locked into a negotiating framework under which they have to wring concessions product-by-product in negotiations with the EU and the US. The outcome is unlikely to be favourable.

This is especially true from the perspective of the rural poor. Trade negotiations inevitably involve trade-offs and hard bargains. The terms on which these bargains are struck are shaped partly by power relations at the WTO, and partly by power relations at a national level. Take the case of Brazil – relevant because it is a G20 leader. In agriculture, the emphasis of Brazilian trade policy is on expanding markets. Some of the country's most powerful political lobbies – in sugar, fruit, and soybeans – are active in shaping this policy through the trade ministry and the ministry dealing with commercial agriculture. Smallholder farmers and agricultural labourers vulnerable to import competition have a far weaker voice in influencing trade policy. So, too, does the ministry dealing with the non-commercial sector. The danger is that any trade-off at the WTO will reflect the priorities of powerful commercial interests, and not more marginalised groups.

Brazil is not an isolated case. It cannot be assumed that negotiators at the WTO have in the forefront of their minds the interests of the rural poor, especially when (as is often the case) the governments they represent have a weak record in prioritising rural poverty reduction. There are no simple answers. However, the limited public awareness of what is being negotiated at the WTO inevitably diminishes the impact of voice of the poor, underlining the case for a greater emphasis on public disclosure and accountability at a national level.

5. Paths ahead for developing countries

The outcome of the agricultural trade negotiations – and, by extension, of the Doha Round itself – remains in the balance. Almost any scenario is plausible. Current improvements in the negotiating climate could lead to an early framework, followed by rapid progress towards full agreement. Alternatively, we could be operating in a period of post-Cancun complacency and heading either for a 'long haul' in the style of the Uruguay Round, or the collapse of negotiations. One thing can be predicted with some certainty, however: in the absence of sustained pressure from developing countries, a WTO agreement will fail to address the problems caused by Northern agricultural policies.

EU–US rapprochement thwarted

Some notable successes have already been registered by the G20. In the run-up to the Cancun summit, EU–US agricultural trade relations followed the Uruguay Round trajectory. Several months of trans-Atlantic sabre-rattling gave way in August 2003 to a joint proposal reflecting a Blair House-style bilateral accommodation of interest. It is worth recalling some of the central features.

Domestic support The Green Box would have been left intact, and the Blue Box subject to weak disciplines. Most US payments would have been exempt from reduction commitments, including those identified by the cotton dispute panel as trade distorting. Blue Box provisions would have shielded the EU from adjustment, and – in one interpretation – given the US scope to remove counter-cyclical and other payments from any reduction commitments.

Export subsidies The language in this area was spectacularly weak. Export subsidies on ‘products of special interest to developing countries’ would be phased out over an undefined period, while others would be reduced.

Market access The joint proposal combined the Uruguay Round and the Swiss formula for a number of ‘import sensitive’ products, leaving large loopholes by setting average reduction ranges, with (lower) minimum cuts.

Special and differential treatment The most notable aspect of the EU–US proposal was an attempt to rewrite the rules of special and differential treatment. It made a fundamental distinction between ‘significant net food exporting’ countries, who would be eligible only for 'adjusted' concessions, and least-developed countries. Even the provisions of the Harbinson text on special products were excluded. While mention was made of a special safeguard arrangement, this was applicable only to 'import sensitive' tariff lines.

Efforts to advance this agenda were derailed at Cancun, principally by the G20 (though not without assistance from EU and US negotiators). In retrospect, it is clear that the EU and the US underestimated both the resolve and the sophistication of the G20's negotiating strategy. Not only did that strategy include the development of an alternative to the EU–US proposal – no mean feat for a coalition spanning major food importers and exporters – but it also encompassed a broader coalition-building exercise beyond the G20. Particularly important in the latter context was a sustained dialogue with the Africa Group and the least developed countries.

African governments played a critical role at Cancun. Questions have been raised about the legality, in narrow WTO terms, of the demands tabled in the cotton initiative by four West and Central African governments. However, the initiative articulated a powerful demand for stronger action on export subsidies, while at the same time forcing the 'special products' approach on to the agenda. At a political level, both the proactive nature of the proposal and the refusal of the four countries to withdraw in the face of considerable pressure from the US marked a considerable departure from the standard WTO negotiating script. It has to be added that the willingness of the WTO Director General to facilitate negotiations on the basis of the cotton initiative framework was an important factor, not least in changing perceptions of the role of the secretariat.

Some important lessons can be extrapolated from this background. Perhaps the most important concerns the future of developing country coalitions. As negotiations move into a more substantive phase, differences will inevitably emerge. African, ACP, and LDC governments remain deeply concerned over the threats posed by the erosion of tariff and quota preferences. Many see the case brought by Brazil and Thailand against EU sugar policy as a statement of hostile intent that will set a precedent. Several G20 members – including Brazil and the Philippines – are in the Cairns Group of major commercial exporters. Other members – notably India – have viewed the demands of the Cairns Group in the area of import liberalisation as a major threat. Both the EU and the US have highly developed divide and rule strategies that will seek to exploit these tensions – witness the European Commission's defence of the CAP sugar regime by reference to the threat posed to ACP interests by trade liberalisation.

Ultimately, the strength and effectiveness of any coalition is determined not just by how it articulates and promotes its shared interests, but also by how effectively it deals with differences. Part of the challenge facing the G20 is to develop strategies for containing differences within the group, and for maintaining in good order the bridges to other groups.

Beyond the Derbez text

Governments of the G20 and other developing countries are involved in a complex negotiating process. Developments in agriculture will inevitably be affected by bargains struck in other areas – on the Singapore issues, for example. Moreover, WTO negotiations in agriculture cannot be viewed in isolation from agricultural policy reform debates in the EU and the US. An incoming US administration will assess its negotiating space at the WTO in the light of how any agreement might affect the 2002 Farm Act. In the EU, negotiations at the WTO are used by advocates of CAP reform to lever change, and opposed by CAP beneficiaries bent on maintaining the status quo.

Developing countries need to assess carefully the interaction between forces driving domestic agricultural policies and the WTO negotiating strategies of industrialised countries. Issues of time-horizon also matter. The AoA of the Uruguay Round has clearly constrained what it is possible to achieve in the current negotiations. Beyond any concrete gains that developing countries might achieve in the Doha Round, it is important that any agreement expands rather than restricts potential gains in future rounds. How might these principles be translated into practice? That question can best be addressed by reference to the four key areas that will ultimately make – or break – a deal in agriculture.

Domestic support

The most immediate aim here should be that of restricting the scope for support that generates export surpluses. Deep cuts in Amber Box support on a product-specific basis and early removal of the Blue Box should be immediate priorities, as proposed in the G20 proposals. Divisions between the EU and the US over the Blue Box create scope in this area for divide and rule in a different direction.

Turning to the Green Box, the G20 is now arguably in a far stronger position than it was before Cancun. The cotton dispute panel has effectively demolished the myth that current payments in this area are decoupled, opening the door to a fundamental review of existing disciplines.

The Derbez text suffers from a number of weaknesses on domestic support. Blue Box payments would be capped and reduced under the Derbez proposals. Their elimination over, say, a five-year period would correct a major distortion. Finally, the Derbez text sidesteps the question of how to tighten Green Box rules.

Export subsidies

This is an area in which the G20 has the potential to bank major gains. There are two layers to the debate on export subsidies. The first concerns the (diminishing) use of direct export subsidies – now concentrated in the EU sugar and dairy sectors – and the parallel use of export credits and food aid by the US. Achievable aims here include:

- an export-subsidy prohibition across all product groups within five years;
- the elimination of the subsidy component of export-credit programmes in a similar time frame;
- a prohibition on the use of food aid for commercial market development.

Here too, there is scope for divide and rule. As a 'non-subsidising' exporter, the US will strongly support moves to cut support, and for an obvious reason: the burden of adjustment will fall on the EU. For its part, the EU insists that any action on export subsidies is contingent on improved disciplines on US export credits and food aid. The Derbez text suffers from acute vagueness on export subsidies. It adopts the EU's language in calling for the elimination of subsidies on products of interest to developing countries, but sets no date for the phasing out of other subsidies. The language also appears to point towards weak disciplines on export credits, focusing on a limit to repayment times. On food aid, the Derbez text merely recites the long-established principle that it should not be used to displace commercial activity.

The second layer of the export subsidy debate is more challenging. Both the cotton and sugar disputes have highlighted the role of direct payments, consumer transfers and other arrangements in cross-subsidising exports. As shown earlier, one of the problems with the current AoA framework is that many subsidies which lower the export price of commodities are not treated as export subsidies. What is needed is a new measure of support to capture this effect – perhaps an OECD Export Support Estimate. Once again, the dispute-panel process has strengthened the hand of the G20 in terms of the range of feasible demands in this area.

Market access

This issue is comprehensively dealt with in another background paper. Here, we restrict ourselves to two strategic questions raised by tariff-cutting formulae and preferences. The current G20 approach is to argue for (i) a strict application of the Swiss formula applied by tariff line, to address the twin problems of tariff peaks and tariff escalation, and (ii) the expansion of tariff-rate quotas. From a negotiating perspective, this raises a dilemma. If the G20 succeeds, presumably with US support in getting a strong commitment to a Swiss formula, the danger is that at least some of its members will come under pressure to apply the same formula. It is certainly difficult to envisage either the EU or the US conceding the application of a Swiss formula for themselves without reciprocal measures on the part of a large group of developing countries.

Turning to the thorny issue of preferences, the challenge for the G20 is to avoid unnecessary division. Some preference erosion is inevitable, whatever the terms of a final agreement: as MFN rates come down, preferences margins will fall. However, conflict can be avoided if major exporters forego the right to challenge preferential access in key areas, notably EU sugar. Such an approach clearly entails financial costs for commercial exporters in the G20, but the political benefits of avoiding divisions with least-developed countries and the Africa group outweigh the costs.

Special and differential treatment

The most pressing concerns in this area revolve around market access and differentiation.

Application of the Swiss formula would create unacceptable adjustment costs. While developing countries may have an interest in proposing this approach for industrialised countries, their own interest is in achieving a weak variant of the Uruguay Round formula for themselves. Many developing country governments may have the flexibility to lower tariffs without fundamentally shifting relative prices, eroding self-reliance, or damaging rural livelihoods. But liberalisation in this area should reflect national policy choices, not WTO imperatives.

Food security is one area in which a one-size-fits-all model is doomed to failure. Distinctions based on country size, export status, average income, dependence on food imports, and so on may be of relevance in many areas, but they are at best weak and at worst irrelevant proxies for food security status.

Developing countries could make a far more powerful case for a WTO regime that allows for flexibility in this area. Far more should be done to highlight the potential threats posed by inappropriate forms of liberalisation. Northern governments themselves face an issue of credibility. It is one thing to advocate open markets in areas where they have some claim to lead by example. It makes less sense to erode the right of poor countries to protect their producers when the EU and the US remain the superpowers of the subsidising world. Diluting special and differential treatment in this context will inevitably be seen as another case of hypocrisy and double standards – and a case that will erode the legitimacy of the WTO itself in the eyes of many in the developing world.

Conclusion

The Doha Round provides an opportunity to address long-standing inequalities in agricultural trade. Bringing Northern agricultural support systems under more effective multilateral rules could create new opportunities for poverty reduction. It would also strengthen the legitimacy and credibility of the rules-based multilateral system.

It goes without saying that major obstacles remain. The negotiating power of individual developing countries is limited – and the vested interests affected by reform in industrialised countries are powerful. Consolidating and deepening the G20 and its alliances with other groups holds the key to progress. While it is impossible to disassemble the AoA framework, in the short- to medium-term there is a strong case for focusing political energies on a number of discrete goals. These include a prohibition on direct export subsidisation, a revision of the distinction between 'distorting' and 'non-distorting' subsidies, and measures to restrict exports of all products at prices below the costs of production.