PECC TRADE FORUM SEMINAR

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Session 6: A Proposal for Progress in WTO Negotiations on Agriculture

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Introduction

First, I want to commend Ippei-san for not listening to me. When he first presented the objective of a PECC consensus on agricultural modalities for the Doha negotiations, I gave him three reasons why I thought it was a bad idea:

1. He had set a June deadline for achieving consensus. I reminded him that 31 March was the Doha deadline so the PECC consensus might arrive too late to aid the debate. Yamazawa-sensei was obviously much wiser than I about the chances of the WTO Agriculture Committee meeting its March 31 deadline.
2. The effort was redundant to a process that Stuart Harbinson had skillfully executed in Doha. (Now having seen a product that is far less satisfying than the Doha declaration, I would say that Mr. Harbinson and the WTO Agriculture Committee could use some additional input.)
3. There are many other technical areas in need of work to which PECC could make a unique and important contribution.

My remarks are not a criticism of the PECC draft document but rather a market analyst's explanation of its components and recommendations for some possible beneficial changes.

31 March

First, it should be noted that the Doha Development Agenda (DDA) was structurally flawed from the beginning. The concept was that built-in agenda items like agriculture should not require a lengthy period to begin making progress. It is a continuation of the Uruguay Round work effort and the issues are quite clear to everyone. That precept ignored the fact that the negotiating round is a "single undertaking" for the reason that concessions in difficult areas like agriculture must be appropriately offset by perceived gains made elsewhere. Politically, certain countries cannot offer up agriculture as an "early harvest" agenda item; the dynamics force a large, encompassing agenda for the Cancun meeting in September.

PECC Precepts

Professor Yamazawa said, "Commitments should be made in an equitable way among all participants. Working with Ippei I realized how difficult it is to divorce oneself from the philosophy of our nationality. He repeatedly admonished PECC Agricultural Trade Study Group participants to not simply represent our national government's position. That is difficult for some of us that have formal advisory roles to our government and feel that the national policy reflects our professional judgement of appropriate policy outcomes. Nonetheless, I will make some concessions for the good of achieving a PECC consensus, while continuing to steer in the direction of the stated objective, "Bringing Agriculture into Competition," and the desired outcome of increased trade.

Multifunctionality and Non-Trade Concerns

No discussion between net exporter and net importer countries would be complete without a debate over multifunctionality and non-trade concerns. I note that the very first issue presented in the paper is not a market opening topic but a discussion about multifunctionality – a concept that does not even appear in the Doha declaration. But its affect on the trading regime would be similar to the concept of non-trade concerns, which is noted at the very end of the agriculture text of the Doha declaration. I believe the draft paper addresses the matter of multifunctionality in a fair manner.

There is no dispute that agriculture delivers multifunctional benefits but the Organization for Economic Cooperation and Development (OECD) has had trouble defining the "jointness" between agricultural production and the associated public goods. There are definitional problems involving calculation methods and the data used. This is why the PECC paper notes that there is a correlated cost/benefit from agriculture on a social value basis but does not explain what it is. Japan has estimated the value of the multifunctional benefits from its rice paddies and upland fields at between $16.6 and $38.2 billion, but has not delineated the actual marginal social value - just the cost of replication. But the cost of replication is not difficult to assume when 90 percent of agricultural support is in the EU, USA and Japan, and only four percent of support in all OECD countries is <u>not</u> tied directly to production.

Net exporters worry about the end game on multifunctionality when they hear complaints that 'the minimum access provided to imported rice under the Uruguay Round has damaged Japan's rice production and, consequently, the country's environmental values.' Rationalizing things such as the "transmission of culture" and "rural amenity" through production-based supports would open a Pandora's box.

The fundamental problem with multifunctionality and non-trade concerns is the "perception" that is all a guise for maintaining support and protection. The reaction from a rational economist would be that market access restrictions and production supports are not the most efficient ways to deliver external benefits such as improved green space. There is too much "leakage" or "less bang for the buck," and it imposes the higher cost of distortions in agricultural markets. One should subsidize the desired outcome.

The PECC paper states that "exporting economies should show sympathy for these multifunctionality and non-trade concerns expressed by importing economies. It will be better attended by mutual understanding and closer consultations between importers and exporters rather than through negotiations." The paper is quite correct since the words themselves are not harmful. Countries can already secure many of these objectives without agricultural support and protection.

The U.S. and Cairns would be more pleased with Harbinson if deeper cuts were made in support and protection. Europe and Japan would be more pleased if Harbinson had recognized their interest in multifunctionality and non-trade measures. Recognition of the latter cannot circumvent the objectives of the former but the latter can be structured in a way that offers something meaningful to the EU (which has already proposed a decoupling agenda for the CAP) and Japan, while achieving the liberalization objective of the U.S. and Cairns. The point is that this is where a political offset must be found in the negotiations, and another area demanding technical analysis.

Food Security and Safety

Food security is a concept unique to net food importing countries and more difficult for net exporting countries to grasp. The U.S. notion of food security is now ensuring that the food supply is not tampered with by terrorists. But the U.S. can relate in the area of petroleum where there is a large import dependence on supplies from relatively unstable suppliers. And this is where the PECC paper contains its most accurate statement in that deciding whether to pursue food self-sufficiency or the more relaxed food self-reliance "depends on the benefits and risks of relying on international trade."

The paper is absolutely correct in asserting that restricting trade for food security purposes only adds to the volatility of food markets. However, it could use some strengthening on export restrictions, which is discussed below.

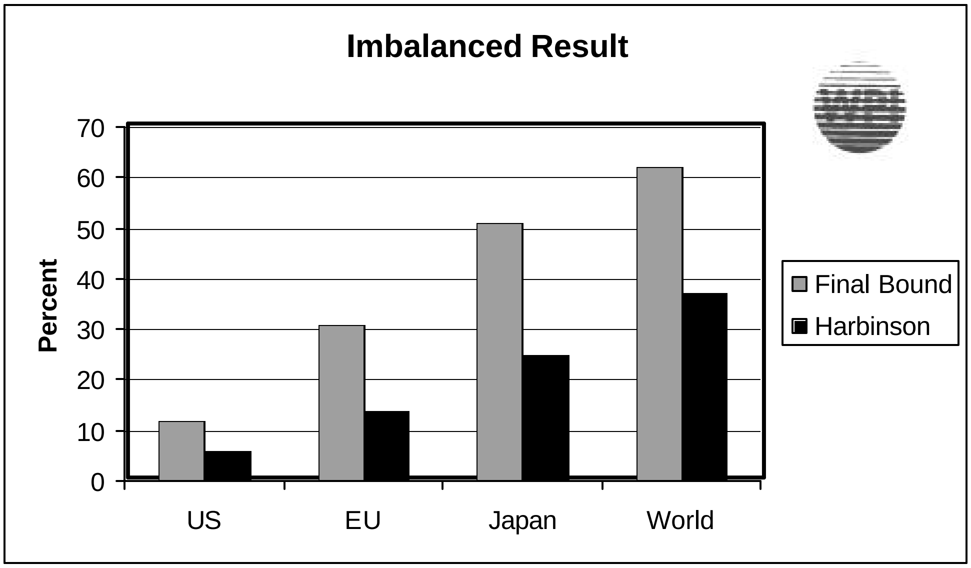
On food safety, the most pressing need is correctly identified in the paper as capacity building. It also warns against overly strict standards that serve more as technical barriers to trade. A quibble should be made, however, with a reference to eliminating pesticide residues. The implication is that chemicals are inherently bad and if this is true, that it should be so stated by the Codex and other residue standard setting entities. Food safety management positions in policy documents should be backed by sound science and not by cultural bias. This is particularly important since a purely cultural bias against chemicals and biotechnology will ensure that not everyone eats.

Tariff Rates

The important point is that we have found global consensus that tariffs need to be reduced; the debate is simply how and by how much. The PECC paper takes a more aggressive position than Harbinson, particularly since it does not create a new class of special products. There are two issues that need to be emphasized: a balanced result and investor needs.

Balanced Result: ." The draft text from WTO agriculture negotiations chairman Stuart Harbinson included large exemptions for developing countries and is being criticized by U.S. farm groups and U.S. negotiators for leaving American agriculture in an imbalanced situation in terms of market access and support relative to the EU and Japan.

WPI Analysis:It is unclear how far and how intently the U.S. will push the "level playing field" concept in terms of the outcome from the Doha negotiations. The argument that the EU should not end the implementation period with greater subsidy and protection authority than the U.S. could gain impetus if Europe is seen as concurrently undercutting U.S. security objectives vis a vis Iraq.



Investor Needs: One problem with trade reform is that some parties do not want to liberalize at all and the other side wants it done yesterday. In the Uruguay Round and now again in the proposals for Doha, the compromise is to partially liberalize over a half dozen years, with slightly longer periods for developing countries. These incrementally negotiated steps provide nearly full-time work for trade negotiators but sometimes fail to move much food. Exporters appreciate liberalization but are not too excited when a tariff goes from 250 percent to 125 percent over six years. Meanwhile, protected industries want to avoid competition but find less objection if the deadline for certain liberalization is far enough away that they can extract the value of their investment and build a cushion.

By providing more ambitious end results – meaning low tariff rates and nearly meaningless production distorting subsidies, the pro-liberalization forces sense meaningful results from the negotiations. Meanwhile, by extending the period for implementing reforms, countries are able to make these larger commitments because the period for adjustment reaches beyond the period in which direct economic or political risk will be incurred. For the protected it becomes like a long-term lease and for the exporter it is the potential benefit of a long-term stock investment.

Differential treatment could be constructed but it needs to have a rationale that recognizes that all countries benefit from global liberalization. A possible extended tariff reduction scenario tied into other policies might look like this:

Developed Countries: nearer-term market access is provided to other countries but domestic supports are allowed for a slightly longer period to ease the adjustment.

Developing Net-Food Exporting Countries: Generally lacking the domestic support programs of the rich countries, they would be allowed a longer period of time in which to implement both their support and protection commitments. (Thresholds are created so that countries like India do not obtain the same special and differential benefits of a country like Angola)

Developing, Net-Food Importing: The longest adjustment period is provided to this group of countries but there is no free pass since liberalization is a benefit.

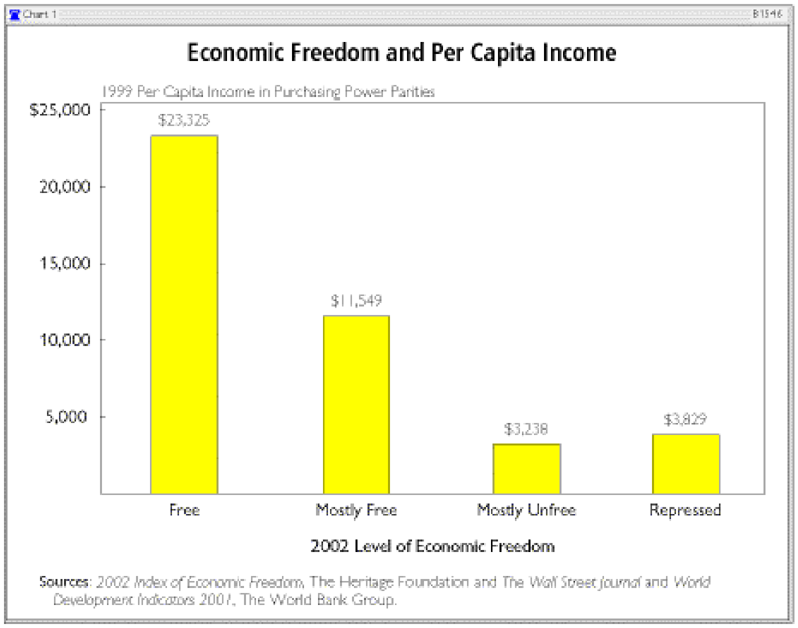
Special and Differential

The WTO negotiations have harbored a philosophical inconsistency in that trade liberalization is good policy and protectionism is bad policy, and so let us allow a longer delay for developing countries to adopt good policies. Developing economies need to be given flexibility but the PECC paper warns against creating a double standard. It advises developing countries to fully accept market competition as they graduate to developed country status. More on graduation is presented below in the technical section.

Trade Alone: We have overburdened trade as the salvation for the developing countries. There are many policy reasons beyond trade that explain why some countries are poor. Fundamentally, the general lack of rule of law hurts confidence, and without confidence there is no business entrepreneurship. This fact is borne out by looking at three different indices:

1. Heritage Foundation/Wall Street Journal Index of Economic Freedom
2. Transparency International's Corruption Perception Index
3. Institute for International Economics FTAA Readiness Index

There is a correlation between per capita income and non-trade specific policies. There is a reason that Haiti ranks 128 out of 156 countries in the Economic Freedom Index, is amongst the worst 20 in terms of perceived corruption and per capita income, and winds up dead last in terms of FTAA readiness according to IIE. Moreover, there are countries at the bottom of IIE's FTAA Readiness Index that have had unfettered access to the U.S. market for years under the Caribbean Basin Initiative. The chart below by the Heritage Foundation depicts the problem:



The flaw in special and differential treatment is its view that economic advantages are best gained through protectionism and favoritism – which ironically are the two fundamental principles rejected by the WTO.

Rich Country Salvation: Another important misperception is that selling to rich countries is the only that trade that counts. According to analysis by the U.S. National Foreign Trade Council (NFTC), most of the duties paid by developing countries (71 percent) is on goods they sell to other developing countries. Developing countries are the growth area for trade but most of the highest applied duties around the world are imposed by developing countries. We note hearing of 1,300 percent tariffs on some goods moving between adjoining African countries - of course the result is simply corruption. Under the DDA concept of special and differential treatment, many of the duties faced by developing countries will largely remain unchanged.

Some keen economists from developing countries have performed Work detailing the importance of developing country agricultural trade liberalization. Eugenio diaz Bonilla of IFPRI who showed that economic value taken away from border protection and instead extracted as a tax and reinvested in productivity gains brings greater and broader economic benefit to developing countries. Marcos Jank, who is here and will discuss the PECC paper should talk about his stellar work for the IDB on the importance of developing country trade liberalization policies. The same analytical outcome was observed by the WTO staff itself at a Geneva conference in May of 2002, but it was apparently politically incorrect for the negotiation leadership to too strongly reflect this fact in their drafts.

Proposal Reflecting Reality: There is a higher cost of delay but the demand from developing countries is for special treatment and it is likely here to stay. The key is to tie together the privileges and the obligations so that developing countries actually make the transition to becoming richer, market economies instead of insoluble basket cases. This means an exchange of commitments between the rich and the poor.

Quid Pro Quo	
Developing Countries	1. Implement economic and political reforms 2. Provide market access 3. Reduce supports
Developed Countries	1. Provide trade capacity building assistance 2. Provide market access 3. Reduce supports

Trade capacity development assistance needs to be provided to the developing countries in coordination with their implementation of obligations. However, it needs to also be recognized that trade alone is not their salvation and that a Doha agreement must be accompanied by implementation of the economic and political reforms that have greater bearing on their well-being than will market access in rich countries for their inefficient agriculture.

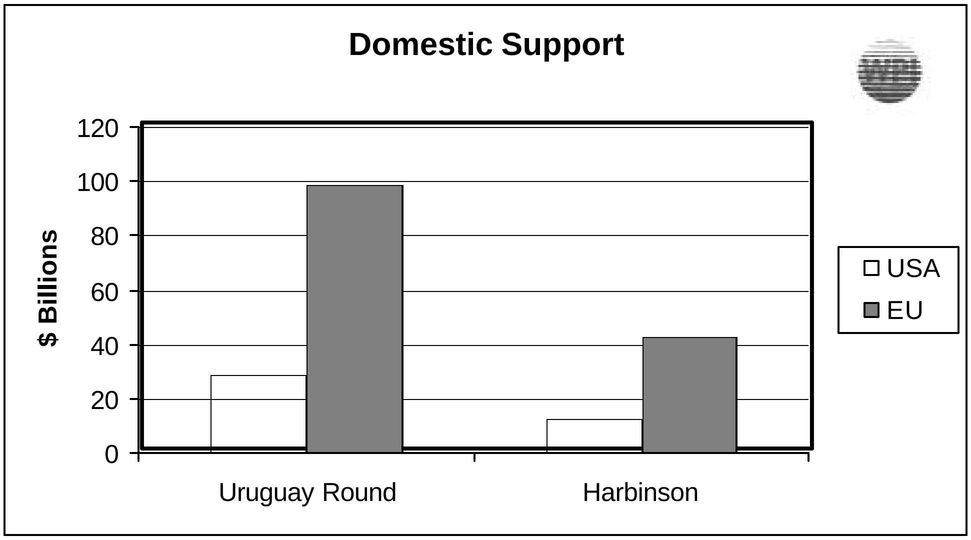
Import and Export STE’s

The Harbinson text, which is an attempt at balance between competing demands, took a definitively tough approach to export state trading enterprises (STE’s), and pressures the import kind by asserting that they cannot nullify or impair market access commitments. The draft PECC position surprisingly changes nothing with regard to export STE’s and uses the weak statement that countries are “encouraged” to shift to private sector trading.

Domestic Support

From a competitive exporter’s position, the amount of domestic support reform is tied directly to the quid pro quo of market access gains. The reference here is back to the investor needs discussion earlier in which both net importers and net exporters would benefit from deeper cuts in support and protection made over a longer implementation period.

The issue of balanced outcome must also be raised here in that following the Uruguay Round's equivalent percentage cuts in domestic support created a disadvantage to all countries that have lower relative levels of support. The PECC draft perpetuates a situation in which the primary beneficiaries are the EU and Japan.



Export Competition

There should be sympathy with Japan's suggestion in the negotiations that the same degree of liberalization should be imposed on net-food exporters (i.e. conversion of all short supply restrictions to export taxes that are bound and then reduced) as the minimum access requirements imposed on net-food importing countries. The PECC draft makes a reasonable attempt at this balance. Where it could be strengthened is in the area of food aid. Contrary to the views of American colleagues, it is reasonable to take the Harbinson approach of saying food aid should be the result of specific requests for identified needs from competent authorities (WFP/FAO), and un-tied and in grant form when not for emergencies.

Technical Agenda

In addition to the PECC's valid input on the main pillars of support, protection and export measures, there is a need to replicate the work of the OECD on tariffication in the Uruguay Round in the new areas that currently divide WTO members. Following are four specific areas that would benefit from further effort in the technical area:

> ***Multifunctionality/Non-Trade Concerns****:* Accommodating EU and Japanese interest in these two aspects requires definitions and impact analyses that mollify concerns by the U.S. and Cairns countries. The OECD needs to complete its definitional work on calculation methods, data use and other factors so that negotiators can better understand their options.
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> ***Green Box:*** If these measures can be used to achieve multifunctional and non-trade concerns, how can this be defined to accommodate EU and Japanese

objectives without impinging on obligations to developing countries? Should there be limits on the amount spent on Green Box measures?

Thresholds: The same level of commitments is applied to all developing countries, yet there are major differences amongst this large class of countries and no clear criteria for graduation to greater obligations. Least developed, "are encouraged to consider making commitments commensurate with their development needs on a voluntary basis." Negotiators need analytical understanding of the kinds of thresholds that might be used to set sliding scales of obligation for reducing the measures of support and protection.

Trade Capacity Programs: Developing countries risk still being poor at the end of implementation periods unless they set strategies for trade competitiveness, and have available the trade capacity programs needed to achieve their strategies. What should those strategies be for each country, and what programmatic guidelines, funding and developed country commitments should be a part of the Doha agreement?